

Draft of Secretary Morgenthau's Speech  
to the Advertising Club of Boston  
September 9, 1941.

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Sept 9, 1941  
9:00 A.M.

Twenty miles from here, at the wooden bridge at Lexington, the men of New England first proved that Americans could defend what they held dear. Today the people of these States are proving that they are still the same New Englanders. Whatever their origin - and they have come from many lands - they are true descendants of the Minute Men. In hundreds of factories and shipyards from Connecticut to Maine, the people of New England are responding magnificently to their country's needs. I am glad to be here tonight to pay my tribute, on behalf of the entire administration in Washington, to the great work that New England is doing to make America strong.

I am glad also that my host tonight is the Advertising Club of Boston, for the advertising profession is a mighty force in creating public understanding. We cannot make ourselves the arsenal of democracy and the defender of

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freedom unless we understand the tremendous issues involved in this Battle for the World. In the same way we at the Treasury cannot accomplish the financing of the defense program unless the public sees clearly the need for greater sacrifice and for greater effort.

In particular, I think it is high time for the American people to become aware of the economic and social danger that must not be allowed to cripple our defense program, the problem that occupies more and more of my time and thought as Secretary of the Treasury, the problem of inflation.

confront a Secretary of the Treasury now a days are not cold and impersonal problems of high finance, they are problems that cannot be solved without a clear, public understanding of the issues involved, and of these there is no problem that occupies more of my time and thought in the Treasury than the danger of inflation which hangs over us tonight.

We have been talking about inflation for a long time as if it were a threat remote from our daily lives. It is a distant threat no longer. We are facing it now and we must deal with it at once.

If we are timid or selfish or shortsighted in facing this issue, the consequences may haunt us and our children for years. But if we are courageous we can beat this thing. If we keep always in mind the interests of our country as a whole, if we provide promptly the appropriate means and

use them vigorously whenever necessary, we can prevent inflation from fastening its grip upon us.

That task calls for alertness and mental toughness on the part of everyone in the executive departments of the Government, everyone in the halls of Congress and every one of us here tonight.

The word "inflation" is cold and lifeless, so cold that even an advertising man might have difficulty in making it real, but the thing it describes is treacherous and cruel. Memories are so short that I suppose many of us have forgotten what happened the last time inflation struck us 25 years ago, but the effects of that inflation lasted for many years and brought untold heartbreak and misery in their train. We are now just where we were in 1916 - on the very edge of inflation. I can think of no subject more worthy of hard thinking on the part of this ~~great~~ audience and of the American people as a whole.

Let us look at the record to see what happened a generation ago. In 1916 the cost of living began to rise sharply but there were few who saw its significance. It was only when prices had risen by 70 percent that President Wilson recommended any steps to prevent inflation. In fact, the country was so blind to its dangers that as late as June, 1917, Congress actually hastened inflation by reducing the reserve requirements for member banks of the Federal Reserve System. By 1920 a ten pound bag of sugar cost \$2.67, a dozen eggs cost 92 cents, a ten pound bag of flour cost 88 cents, a pound of butter cost 76 cents and a pound of pork chops cost 50 cents. By that year prices had skyrocketed to twice the level of five years earlier. The money the housewife paid for one loaf of bread in 1914 bought only half a loaf in 1920. The money she paid for a pound of bacon in 1914 bought only half a pound in 1920. The money she paid for a yard of cotton cloth was only enough to buy only 1/3 of a yard

in 1920. The family with no increase in income found its purchasing power cut in half. It found <sup>that</sup> food, fuel, shelter and clothing that cost a dollar in April, 1916, had risen to almost two dollars by 1920.

We have now, as we had then, a moderate rise in the cost of living, a great rise in wholesale prices, and a still greater rise in the prices of basic commodities like wheat, hogs, cotton and lumber. It is <sup>the</sup> rise in the prices of basic commodities that constitutes our danger signal today, for they are always the advance guards of a rise in the cost of living.

If prices continue to rise as they did from 1916 to 1920, we shall find that food, fuel, shelter and clothing that now cost a dollar will once more cost almost twice as much before the process has ended.

The rise in prices is by no means confined to food-stuffs and clothing. I have before me, for instance, the actual figures on the cost of constructing a standard six-room frame house in one of our typical cities. This home that could have been built a year ago for \$6,000 now costs \$7,140 to build. Here we have an increase in prices of nearly 20 percent and if it goes along the 1916 pattern, we are only at the beginning of the story.

Not only is the cost of building homes rising but even for the millions who do not own their homes higher rentals are on the way. We find already in scores of areas where industrial expansion has first taken hold, rents rising 10, 20, 30 percent and even higher.

There is, however, one great difference between conditions today and 1916. We now know what is going on. This time our

eyes are open to the dangers that lie ahead of us. We now know that the time to do something about inflation is before it occurs, not after it has gathered momentum. We should profit by our greater knowledge and take prompt and effective action now.

There is no need for me to remind this audience in detail of the reasons why prices have already risen. The reasons are plain for everyone to see. Our economy today resembles an overloaded steam boiler. The fire under the boiler is being fed by billions of additional purchasing power in the hands of the public. The fire is growing hotter and is generating more steam than the boiler can safely hold. If we are to prevent the boiler from bursting, we must damp down the fires by withdrawing purchasing power, and we must also enlarge the boiler by increasing the supplies of goods available to the consumer.

In speaking of these things I am not being an alarmist or defeatist. We can, as I have said before, defeat this threat, just as we can lick the forces of evil that have been let loose upon this earth. But we need to understand the issues and we need to see clearly the consequences of inaction or delay. I should like, therefore, to look at the problem quite coolly for a few minutes, to see <sup>first</sup> what we have done ~~and~~ ~~what we need to do~~ <sup>and then what we need to do</sup> in order to stop prices from rising further.

In the first place, Congress is on the point of passing a huge tax bill designed to raise almost four billion dollars in additional revenue, thus withdrawing a great amount of purchasing power that competes with the defense effort.

Secondly, the Treasury in its borrowing program is trying to obtain as large a portion of its funds as possible from current consumers' income. Through a new form of note - the tax anticipation note - it is seeking to increase the

effectiveness of the income tax as a check on current purchasing power, and I am happy to report to you that more than a billion dollars' worth of these notes were sold in the month of August.

The Treasury has also begun a program of selling Defense Savings Bonds and Stamps to people of moderate and low incomes. The people have responded to a tune of a billion and a quarter dollars in four months, without coercion of any kind; and in that response the people of Massachusetts and of New England generally have stood in the forefront.

The President has recently issued an order authorizing the Board of Governors of the Federal Reserve System to control consumers installment credit. The Congress is considering, and I hope will pass, a bill to limit price rises and to supplement the efforts of the Office of Price Administration, to limit price rises by voluntary cooperation.

All these are useful steps to a necessary end, but they are not enough. We may have to extend general controls over bank credit and create controls over selected capital expenditures. I hope that we may extend the social security program *so as* to increase the flow of funds to the Treasury from current income during the emergency and increase the outflow of funds when needed in the post defense period. We shall have to reduce the Federal lending and underwriting program such as non-emergency housing expenditures and mortgage guarantees. We must, as I have said many times, reduce nonessential Federal expenditures. We must also appeal for economy in state and local government expenditure and a curtailment of their borrowing for nondefense purposes.

All of these measures would attack the problem by attempting to reduce the demand for goods now and by helping to build up a backlog for the post war world. But we should also attack the

problem from the opposite direction by making every effort to increase the supply of goods available to the consumer wherever this can be done without encroaching upon the defense program. Above all, we must make full use of those supplies that are available not only in defense production but in the civilian goods which do not compete with defense output.

I wonder if the housewife knows when she pays 20 percent more than she did a year ago for a bag of flour that our supply of wheat is the largest on record, and that 498 million bushels of two years' crops are stored in Canada. I wonder if she knows when she pays 15 percent more for a pound of sugar than a year ago that there are unusually large sugar stocks in this country and in Cuba. I wonder if she knows when she pays 25 percent more for butter, that we have great stocks of butter in storage, and large reserve stocks of

farm products of many kinds which should be released for consumption as fast as necessary to prevent unreasonable price rises.

The Government now owns 7 million bales of cotton in reserve, and cotton prices have risen from  $9\frac{1}{2}$  cents a pound on August 1, 1939 to over 16 cents a pound at the present time. We ought not to withhold surpluses from the market in this manner. The housewife ought not to be made, in times like these, to pay a tribute to profiteers and speculators when she buys a cotton sheet for her home or a shirt for her husband or a suit for her child.

Millions of people still go without the milk, butter and eggs which nutrition experts have found necessary to good health and good morale; yet we are withholding the largest reserve of milk, butter, eggs and cheese in our history.

I know from experience on my own farm that within two months

we could increase our supply of milk by feeding some of our huge surplus of corn to the cows. I know that we could use some of our surplus grains as feed for chickens and get more eggs, yet the price of a standard poultry ration has increased 60 percent since the war began. This has been historically a land of milk and honey. There is still plenty of milk and honey but too much of it is in the warehouse. Let's make it flow. If we were to let it flow to the public we would not only help in keeping prices stable but we would be doing something even more important; we would be helping to make our people healthier and happier.

It is sheer folly from the farmer's point of view to be pushing prices up by creating scarcities in times like these. The farmers suffered cruelly for twelve long years after the collapse of the inflation of 1920 and 1921. It is sheer folly in the same way for labor leaders to seek continual increases

in wages which in turn produce higher manufacturing costs, higher prices, and a higher cost of living. It is shortsighted for landlords to charge all that the traffic will bear in cities where housing space is at a premium because of defense needs.

There are always selfish groups in any country which think they can profit from inflation. They are ~~dead~~ wrong.

Inflation does more than merely to rob the wage-earner of a portion of his earnings. It does more than saddle the farmer with a load of debt which he cannot repay. It is more destructive of morale than any other single force.

Inflation divides the country. It sets up producers against consumers, workers against employers, the people who owe

money against the people/<sup>to</sup>whom the money is owed. No group

in a community profits from inflation in the long run except

THE THREE HORSEMEN - THE SPECULATOR, THE PROFITEER AND THE

HOARDER.

These are truths that should be self-evident. They should be especially so now, in view of the fact that rising prices will only add to the cost of our defense program and make the arming of our country steadily more difficult. They should be self-evident now in the light of the experience that we suffered only 25 years ago.

You in New England have 300 years of experience behind you. The American people as a whole have 150 years of self-government behind them. We are not children any longer. We are a mature nation, and we should be able to face up to our responsibilities as mature men and women. My plea to you tonight is that we should learn from bitter experience. My hope and my belief is that no group among us - whether farmers, working men or business men - shall be tempted by the illusion of selfish gain into allowing prices to rise unchecked. The cost of inflation is too ruinous to producer and consumer alike

for anyone in authority to tolerate it now. I can give you only this pledge - that we at the Treasury will do everything humanely possible to check the rise in prices before it will do any lasting damage to our economy. But we at the Treasury must have the firm support and the clear understanding of 130 million Americans behind us. If we have that support and that understanding, I know that we shall not fail.

September 3, 1941  
10:15 a.m.

RE EXCESS RESERVES

Present: Mr. Bell  
Mr. Stewart  
Mr. Bernstein  
Mr. Haas  
Mr. Murphy  
Mr. White

H.M.Jr: Well, now, Dan, how will we run this thing?

Bell: Well, I hardly know. Have you read George's memorandum?

H.M.Jr: Very hastily.

Bell: It is a good memorandum, and personally I agree with him.

H.M.Jr: Everybody come closer. Come within my ten-foot vision.

Does somebody want to take the argument, why we should do what the Federal Reserve wants us to do? Will somebody take that side?

Stewart: Well, I will make an observation. I think the memorandum is a good memorandum. I think it is very persuasive, and I think it is particularly persuasive because it really comes to a conclusion quite convenient to the Treasury. I don't mean that to be funny. I mean, it is

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one of those cases where it is awfully difficult to come to any other kind of decision. I think it depends on how seriously you take the threat of inflation, and I take it seriously. I think it depends--

H.M.Jr: I take it terrifically seriously.

Stewart: I think the next step is to say where you think the inflation is serious. I think, among other places, it shows itself in the bond market now. Now, if you look back on these periods of incipient inflation, the action is always too late. This has a reminiscent quality. There are two experiences we went through.

H.M.Jr: Just one minute, for my speech. You are quoting Lloyd George.

Stewart: That is right.

H.M.Jr: "Too late moving here, too late in arriving there, too late in coming to this decision, too late in starting enterprises, too late in preparing for this war, the footsteps of the Allied forces have been dogged by the mocking specter of 'too late.'" That is the quotation.

Stewart: It certainly applies to all these problems of monetary control.

H.M.Jr: The way you put it, "too little and too late."

Stewart: That is right.

H.M.Jr: Well, they have been using it, but that is the quotation.

Stewart: I was thinking of two earlier periods in our experience. There is the 1919 post-war period

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with the Treasury on one side and the Reserve System on the other, chiefly.

- H.M.Jr: Is that a public document?
- Stewart: That is in the files. There was a long correspondence. At the time it was rate control, the question of rates and when rates ought to be brought up.
- Bell: Just before the Victory Liberty Loan.
- Stewart: By 1920, yes, a collapse.
- H.M.Jr: Now, what is the position that Treasury took?
- Stewart: Treasury at that time was arguing that the Federal position was not unsound, that it had this financing to do, that it would be at unnecessarily higher rates. They could carry through on the war basis and Strong was arguing for the immediate correction of the discount rate in New York. I don't pretend that that is the only factor in that position, but the correspondence is long and well written.
- Bell: Yes, it is good.
- Stewart: It is good correspondence.
- H.M.Jr: I thought at that time that David Houston was blamed by the farmers for the collapse of the twenties.
- Stewart: Well, Harding did as much of it as anybody did during those days.
- H.M.Jr: What were the steps taken?
- Stewart: The real incipient period, or at least the climax on top of the war period is the period that comes in the Victory Loan in 1919.

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H.M.Jr: Well, you see I am not - I have never studied that. It was when, in--

Bell: It began in January, I think, 1919.

Stewart: Right after the Armistice and the demobilization you have got this period of cleaning up the accumulated indebtedness.

H.M.Jr: Is that a very long correspondence?

Bell: Yes, quite a bit.

H.M.Jr: How much?

Bell: Oh, it is a file about an inch or so thick.

H.M.Jr: Couldn't somebody digest that for me? I wish you would have it done promptly and then have references in case I want to do it some more. That was in connection with the Victory Loan. How big a loan was that?

Bell: That was a four and a half billion dollar loan.

H.M.Jr: What rate?

Bell: There are two issues of Victory Notes, one of three and three-quarters and the other of four and three-quarters.

H.M.Jr: Did my interrupting spoil your thought?

Stewart: Not a bit.

H.M.Jr: Go ahead.

Stewart: Well, the other period, and it is not unlikely, is the 1928 period, controversy between the Reserve Board and the New York bank at that time. The Reserve Board was arguing for direct action as against rate action. The New York bank

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argued for rate action. Again it was a sort of division in monetary authorities. Now looking back on both those periods, the time is lost when you say it is too late. It is the time consumed in discussing which method ought to be used. They really should have done both things.

H.M.Jr: Done what?

Stewart: Both the direct control and the rate.

H.M.Jr: What is the direct control?

Stewart: The direct control is the thing George argues for here, a selective process. In 1928 it was the security loan. Now it is giving way for the defense industry and shutting off the non-defense industry. It is perfectly rational. But it isn't to my mind entirely persuasive that at this stage one ought to choose between methods before one closes the book. One ought to see whether or not both methods may not be necessary and desirable.

H.M.Jr: And therefore you lean--

Stewart: I am not yet ready to say in view of all the implications and using the Reserve restrictions that that is what I want to do at this moment. I do say just at the first reading of this - I haven't read the Federal Reserve memo or talked with George - I do say I would not shut off the possibility of doing both things if I took inflation seriously.

H.M.Jr: I haven't read the Federal Reserve memorandum. What was it?

Haas: I just got it.

H.M.Jr: I asked them for one, didn't I? I asked Gaston

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to ask them for one.

Haas: I wasn't here and Henry did it and--

H.M.Jr: You see, when I heard this last week - I sense these things. I heard about it, and I said, "Well, get the Federal Reserve to give us a memo and get Haas' shop to give us a memo and we will sit down and thrash this thing out, because I take it very seriously.

Stewart: I thought you did.

H.M.Jr: This is the way I feel without having gone into the ground work too thoroughly. I would be willing to increase their reserves by the maximum, irrespective of what it costs us in our borrowing, if I was convinced that by doing that I was really foresighted, you see. The thing that - and then the other thing, on the small end of it, the personal end of it - there is always the human element that enters into it. We are all small. Having them in on that is the next move that they want, legislation to have much further control, you see.

(Secretary held an unrecorded telephone conversation with Miss Grace Tully.)

Stewart: You know, we humans that you refer to were equally present in these other episodes to the point where friendships were broken. Men who had had long associations with each other felt quite bitter, and for long years--

H.M.Jr: You see, all of this is a closed book. If I can draw on you for the experience--

Stewart: Well, I think that this is the time where prospective is entirely unimportant. These personalities disappear. But you do find them in the action that is taken. I think any

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correspondence or action that is taken has to put the Treasury's position in such a fashion that it has the farsighted concern. You can put it and say, "I don't believe that such a policy, viewed in the long run, is a wise thing to do because of its implications." You can't ever afford to say that you wouldn't do it because you would pay a low rate. You can't afford to do that.

H.M.Jr: But you see, I am going to let you read this draft of my talk which covers the whole field of inflation and it is finished. If you care to listen to it, I will give you a chance to hear it tomorrow morning, but I want to let you know how serious I am about it.

Stewart: How seriously do you regard inflation in the bond market? Prices are higher and yields are lower than it will be possible to sustain them in the light of the present prospective developments. That is a definition of inflation, to me.

H.M.Jr: Well, let me put it this way. The price of the bond market has been high and interest rates have been low long before we had national defense. Right?

Stewart: Yes.

H.M.Jr: So we can't compare the - I mean--

Stewart: But you introduce a new element of national defense. That is one of the factors in affecting one's judgment, as to the capacity to sustain that level of rates.

H.M.Jr: Well, let me give you - make a statement which is not an answer to your question but bears on the point.

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What I was trying to answer you was this: If we are going to do something like this three months from now or six months from now - in other words, you get the bond market to give it a shock and see just what will happen to it, there will never be a better time than right this week. I mean, if we are going to do this thing, I will say I doubt if we will ever have a better time for the rest of my term than right now. Now, it is like the President - he cancels the cotton bill freezing and cotton goes up, so we might - if we are going to do something about reserves, I say for God's sake let's do it now and see what happens and see whether the bond market is or isn't inflated. That isn't reasoning, but it is the old elbow, and I won't have a better chance, because I have got a working balance of just under two billion, and I can take it in my stride, and I can go on either with bills or notes and see what happens. So, as I say, that isn't--

Stewart: The time is appropriate.

H.M.Jr: Nothing scientific, but what I am trying to answer you is, I am not afraid to do this thing. Now, let's say we do this thing, and let's say that the bond market takes it in its stride. Well then, it isn't inflated. If it goes down four or five points, then it is inflated. I don't know. Of course, the last time they did it, it took them eighteen months to get over it. They went - it was about eighteen months that we had a bad bond market, wasn't it? Life insurance bought what the banks sold and saved the day. They did it practically dollar for dollar. I realize perfectly what I am saying, but I feel this way, that if the Fed feels that this thing is an inflated market and enough people around here feel it is deflated, and they want to squeeze

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the water out, now is the time to do it. I don't want - I have got too many things, and I don't want this thing hanging over my head. There has been enough talk. It has all been written up in the press. I mean, somebody in the Federal Reserve System has been talking. The other day I heard this woman, Sylvia Porter, in New York with a whole story on it. Goldsmith in the bond letter had the thing, so it is all out.

Bell: Everybody is talking about it.

Stewart: It is hanging over everybody's head.

H.M.Jr: And as I say, I realize I am not being very scientific.

Stewart: That is the only science I know is to test the market and what you would do, you would say this is the most convenient time to make a test. There isn't any other wisdom possible. Everyso often you have to test it to find out whether or not it behaves right.

H.M.Jr: They can raise it about another billion dollars?

Haas: A little over a billion, reducing from five to four the excess reserves. But the market would want to know if that ends it, whether you would want to join with the Federal Reserve is to ask for legislation to give them more power, you see, and if they think this is just the beginning of it, that is one thing, or if you are going to give assurance that ends it and from there on you are going to use selective controls, that is another problem. And if you give it a drastic crack, the Federal's staff and the Board feels that the way to handle the

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bond market is to control it through tap security and they handle the whole market by buying back and forth.

H.M.Jr: What kind of security?

Haas: Tap securities.

H.M.Jr: What are they?

Haas: In other words, continue a sale. You continue as tap or continue as a sale. They control the market. It seems to me that if this is artificial, what we have got now, that sort of thing is just making trouble and putting a distinctly artificial situation in where it is not required at all.

Bell: It seems to me if we are going through with it then we ought to let the market alone and let it settle to its level and not have the Federal Reserve try to peg the rate at two and a half percent.

H.M.Jr: Did you say that in the memorandum?

Haas: Oh, yes.

Murphy: They suggested a memorandum that they wrote

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this thing, that it would be well to get it marked down in one piece so the climb wouldn't hang over, and it simultaneously would increase reserve requirements. We should put out a tap issue of three to four percent, offer an unlimited amount of it, and thereby cause the market to drop off like a precipice, after which it could be stabilized for good.

H.M.Jr: At three or four per cent?

Murphy: They say three dash four.

Haas: And I question whether it will be an important factor in it - in controlling inflation. In other words, if you are going to do this, the memos from the staff - Goldenweiser mentioned it in his, but the other - you have got to have these specific controls on top of this other one to really control inflation, because all the commercial ones they will go ahead and the Board will continue on. An increase in rate won't defer them any. People will pay it. So if this solves the problem you could say, "Well, now, inflation is under control. We have it in the bag. We made this sacrifice." That is one thing. But if you go ahead and run the rates up to three or four per cent and then you still have your inflation problem on your hands, you will find out, and I think you have got to weigh it very carefully.

H.M.Jr: The reason I say what I did is, I am willing to remove all personal feelings out of this thing and just set them aside. I have never permitted myself to let personal feelings interfere with our welfare. If I am convinced this is the right thing to do, hell, let's do it. You have never heard my--

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Bell: No, that is right.

H.M.Jr: If a fellow has got some deep feeling that this is the way to do the thing and this is going to end it, and it is right, then do it.

Stewart: I am in the same mood. This doesn't answer the problem. The only question is whether or not there aren't a multitude of things you will have to do.

Haas: We might compromise and go the limit if they could give assurances that from then on it will be used for specific controls.

Stewart: Do you want that sort of thing?

Haas: That is it. That practically ties the Federal Reserve and says, "From then on you mean nothing."

H.M.Jr: Again, to get on the personal basis, you don't know who is doing the thing over there? Is it one man or is it a group? Is it the Board together?

Bell: I think it is the Board.

Haas: Draper, I think, dissents, isn't that right?

Murphy: I gathered that impression when I was over there. He didn't say so in so many words.

H.M.Jr: Were you over there?

Murphy: Yes, sir. I met with Draper and Szymozak and Clayton and Thurston and Thomas and Piser and Longstreet. I had intended to meet those people at Mr. Gaston's suggestion. He asked me to get in touch with them. I called up Thomas and when I came over he had that group assembled.

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H.M. Jr:

Here is the thing that isn't clear in my mind. I know there are a great many forces which are working for higher prices and locking up this money, I just don't see how that stops people from wanting to spend the money on non-defense articles. Now, I wish somebody would explain it to me.

Stewart:

It doesn't. It deals with one area of inflation, to my mind, which is the bond market. The Government bond market is a base line for every other article in the bond market. The result is that if it is inflated it tends to create the same position all the way through, so that either during or after the war you have a problem of the readjustment of your base line, whether your base line is near enough in line with what you expect to be able to carry through - let's put it the other way around. Suppose we say, "Well, this rate is all right. Not merely - I don't mean to test it, but we have a capacity and it is good. Take two or three per cent rate, carry the financing through on it, and hold that position post-war, so that you say, "This is a pegged thing." Now, my own belief is that it is an extremely difficult art in the long term money market. I think one of the weaknesses in currency is the management of this long term rate over a long and indefinite period. Therefore, I believe the present market to be inflated, but I wouldn't go beyond saying that this is a correction of one of the places where I think it is inflated and therefore do it for readjustment at some time, and I would rather have the readjustment at some convenient stage than I would after I had had another thirty billion of debt accumulated and in the hands of the public. I don't think a war of this magnitude can be conducted on a two per cent basis or a two and a half per cent basis.

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- H.M.Jr: Well, let's say that instead of two and a half we go to three. How does that stop inflation?
- Stewart: One half per cent better. One half per cent less readjustment, which is ten points.
- H.M.Jr: But how does --
- Stewart: It doesn't. That puts you into a whole area of what we all mean when we talk about inflation, which is so wrapped in mystery and logic and subterfuge.
- H.M.Jr: But let me get this thing straight. If what these people are worrying about is the readjustment after the war, that is one thing. Or if it is that they feel that the present price of bonds is too high and the price should be driven down, that is something else.
- Stewart: Are some of them saying that?
- H.M.Jr: I don't know. Here is the thing. Supposing we say, "We will do this." All right, we increase the reserves and lock up another billion dollars. That is what we do, isn't it?
- Stewart: Yes.
- H.M.Jr: Make the banks hold it. And then we go and get out what, a long term issue on the new basis? That would be one way. A three per cent issue. Or I say I am not convinced that the price of bonds is too high and I don't want to sell any more long term issues because I am not sure. Therefore, I get out a five year note. That increases reserves because it will go solely to the banks, won't it?
- Stewart: Increase the deposits, yes. There is no question about it. You have got a much more difficult task here than existed in either of the other two episodes.

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- H.M.Jr: Couldn't you have an in-between thing and say, "All right, instead of giving the bond market a terrific shock, let's have a creeping interest rate. Let it go up gradually.
- Murphy: No one likes to buy bonds on a creeping interest rate.
- H.M.Jr: Of course the answer is that they will if they can't get anything else. That is the trouble. You have got to be terribly frank with each other. The trouble is, there are no new money bond issues.
- Stewart: Anybody in the banking business that shows a loss on a book value of an earlier issue, that slows down a new issue --
- H.M.Jr: But the trouble is, I think if you go through the last - back to the first of January -- just do it for fun, I mean not now. See how many new issues were brought out as bond issues. I doubt if there have been a hundred million dollars.
- Stewart: Of new money?
- H.M.Jr: Of new money, Henry. Now, the fellow is faced with this. He says, "I have got to earn my salary and my payroll and I may take a loss but I am going to buy these Government bonds anyway, although everything tells me I shouldn't." So he goes against his better judgment and we force his hand.
- Stewart: He goes a little longer than he meant to go in order to get the yield.
- H.M.Jr: If this is all right, it is too high. We had that fellow from Baltimore, remember? He was a smart old fellow. What was his name? That bank?

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- Bell: McAdams of the Baltimore Trust?
- H.M.Jr: Well, he just - they tell me he is one of the smartest trading fellows. He spends a lot of time on his three farms, but he sat here and told us - called a spade a spade, didn't he?
- Bell: Yes, he was very frank.
- Murphy: There is quite a time factor, though, Mr. Secretary, while the acquisition of income may be ultimately necessary, you can always temporize with cold cash, and it seems to me that bond buyers generally are much more ready to buy on a low market or high market than on a falling market, and that a falling market, gradually falling, creates a very bad environment for selling bond issues.
- H.M.Jr: Here is the way I feel. This thing isn't - the trouble with the damn Federal Reserve memos is that they are so long.
- Haas: This is very short. He didn't want to put it on that level, he said, so he addressed it to me, but I think he hoped you would read it.
- H.M.Jr: Is it short?
- Haas: Two and a half pages.
- H.M.Jr: Where is it? It only came this morning?
- Haas: Last night.
- Murphy: About six o'clock.
- Haas: I will give you the whole batch.
- Bell: Whose memorandum is this?
- Murphy: I don't know. It was given to me by Thomas as an academic discussion, a rather thorough discussion of the matter. It was written by

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them in the spring. I found it quite interesting. It is in that memorandum that they say, "If you are going to raise the rates, you ought to raise them fast."

Haas: I think it comes down to this, Mr. Secretary, what Walter Stewart mentioned. Is this rate too low? Do you want a higher rate? Doing it isn't going to be an important factor in inflation. In fact, these memos that you have there, they indicate that to do this with gold inflation you have got to increase your taxes much more. You have got to put in forced loans. So what you wind up with, you do this as a method of raising the general interest rate and then do all the other things that are necessary to control inflation, including these selective controls. Isn't that right, Walter, doesn't it come down to that?

Stewart: That is the only thing you can argue, it is to diminish the magnitude of your task. You somewhat make your total task easier, though you see by the same methods it won't be easier in the long run.

H.M.Jr: A lot of these arguments in the memorandum are out of date. There is no criticism today of the banks extending credit. They are doing a beautiful job. You would think he was writing this two years ago. How much have the banks increased the loans?

Haas: About two billion eight hundred million, but that is inflation, too. That has to be improved.

H.M.Jr: Another thing, I don't like, "The decision must be made to support the rates selected."

Haas: That is the tap.

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H.M.Jr: That is just as artificial as anything else.

Haas: I think it is more artificial.

It is a rate peg in the market. They look at it and the Government's credit is standing on its own feet.

H.M.Jr: I don't mind saying I think that is a very, very weak memorandum. I mean, I would state his case much better than that. He stated it very badly, don't you think so?

Stewart: Yes, I think the mood to approach this in is that --

H.M.Jr: I think it is terrible.

(Mr. White entered the conference).

I am terribly disappointed. I would state it better than that.

Stewart: It is rather different from the others.

While there were differentials of monetary authority, the real control is here.

H.M.Jr: It should be, shouldn't it?

Stewart: Yes, it is all right. And the real borrower is here. So you have got a peculiar two-fold responsibility. Entirely apart from the motives with which this sort of recommendation is made and what else they have in their mind, personalities, whether the arguments are good arguments, all I say is that this is a good time to be aware of this responsibility and appraise it in the light of prospective problems instead of the immediate situation.

Haas: Mr. Secretary, did you notice the British press comments on the January statement of the Board?

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H.M.Jr: No.

Haas: I have forgotten whether I sent those in. They came over in a pouch from the British Embassy. That is the type of headline they had. There were several papers of the same tenor all the way through.

H.M.Jr: I will tell you what I would like to do, Dan. Could you get this group together maybe this afternoon?

Bell: This group?

H.M.Jr: Yes. and do a little more threshing around. I don't think we have done enough of that in our own place and --

Bell: We haven't read any of this stuff from the Federal Reserve. We just got that. Unless George read it.

H.M.Jr: I won't have a chance, unfortunately, to touch it again until eleven tomorrow, but if anybody gets any ideas --

Bell: You have got a conference at eleven.

H.M.Jr: With these two men, tomorrow.

I don't mind talking perfectly frankly before them. I think, Walter, - and Viner is here. You might send him - he will be here tomorrow. You might send him a wire to be here at nine fifteen tomorrow.

Bell: Isn't he coming?

H.M.Jr: He is coming. He will be here.

Bell: I thought he would be here.

H.M.Jr: That is right, he will be here.

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Bell: Who notified him, Mrs. Klotz?

H.M.Jr: I notified him to be here tomorrow. He will be here.

Well, I just think if you could get this group together this afternoon - Harry will have to be excused because he is working with Kuhn on this other thing. O.K.? I mean, don't you think - and just remember this. If we are going to do it, now is the time to do it.

Stewart: Yes.

(COPY)

September 2, 1941

Secretary Morgenthau

Mr. Haas

Subject: Excess Reserves, Credit Controls, and Treasury  
FinancingSUMMARY

This memorandum is prepared at the request of Mr. Gaston made following a telephone call which he received from Chairman Eccles while you were away. A copy of Mr. Gaston's memorandum to you summarizing his conversation with Chairman Eccles is attached hereto.

Chairman Eccles asks that the Treasury concur with the Reserve Board in raising reserve requirements to the present statutory limits and in requesting from Congress a further increase in such limits. He recognizes that such action will depress the market for Government securities, but believes it necessary in order to combat inflation. He urges, therefore, that long-term financing be deferred until after the announcement of such a program in order that both the Treasury and the Reserve Board may be spared any accusation of bad faith.

Excess reserves now amount to about \$5.0 billions, a decrease of \$1.9 billions since the all-time high reached on October 23, 1940. Barring changes in official policy or the import of substantial amounts of gold from Russia, total reserves appear likely to fluctuate within a narrow range for the next year or so. Any further decrease in excess reserves, therefore, is likely to come only from an increase in required reserves due to continued deposit expansion.

Such transformation of excess reserves into deposits -- at a ratio of about \$5 of deposits to \$1 of excess reserves -- would be inflationary, rather than deflationary, in its implications.

While the immediate effect of raising reserve requirements is to increase interest rates, its stated objective is to combat inflation. This objective would be achieved in some degree by the mere psychological effect of the increase. In order to be of permanent value as an anti-inflationary measure, however, an increase in reserve requirements must result in squeezing some borrowers out of the market. This would be done by making borrowing more expensive and so causing the Government and the defense industries to compete with other borrowers on a price basis. This naturally leads to the question of whether an increase in interest rates is the best method of squeezing non-essential borrowers out of the market.

A consideration of this question leads to the conclusion that the direct exclusion of non-essential borrowers from the market would be preferable to exclusion by rate competition. Selective credit controls -- such as control of consumer credit, of housing credit, of new capital issues, of stock exchange loans, and of bank loans for non-defense purposes -- appear, therefore, to be superior to the general credit control proposed by Chairman Eccles.

It is consequently suggested that you should not concur in Chairman Eccles' request that you join with the Reserve Board in recommending an increase in reserve requirements. In such a case there seems to be no reason to defer long-term Treasury financing beyond the time when it would otherwise be advisable.

#### I. Chairman Eccles' Proposal

On August 22, Chairman Eccles called Mr. Gaston to express his hope that the Treasury would offer no long-term securities in September or at any time up to December, but that such new money as might be required in the meantime should be procured by means of Treasury bills. A copy of Mr. Gaston's memorandum

to you summarizing his telephone conversation is attached hereto. Mr. Gaston requested us to consult with members of the staff of the Board of Governors concerning Chairman Eccles' proposal and to prepare a memorandum to you.

Chairman Eccles' reasoning is as follows:

The present level of Government Bond prices is justified only by the existence of a large volume of excess reserves. It is desirable in the interest of the control of inflation that this volume of excess reserves be reduced sharply. He would like to have the Treasury concur with the Reserve Board in increasing reserve requirements up to the present statutory limits and in asking Congress to increase these limits, thereby giving the Reserve System authority to increase reserve requirements yet further. These actions would probably cause a substantial decline in the bond market. He is particularly concerned about this decline in the case of the two new long-term taxable issues, as he believes that the tax-exempt issues and all short-term issues can take care of themselves. He is very anxious, therefore, that no new long-term taxable issues be put out at the present level of the market. To do so at this time, and shortly thereafter to take the action which he considers necessary with respect to reserve requirements, would, he believes, subject both the Treasury and the Reserve Board to justifiable accusations of bad faith.

Chairman Eccles' views appear to present the following questions:

- (1) Is it desirable to increase reserve requirements at this time?
- (2) If this is not desirable, should any alternative measures be taken?
- (3) If reserve requirements are to be raised, should long-term financing be postponed until such action has been taken or at least recommended to Congress by the Reserve Board and the Treasury?
- (4) Could the Treasury finance itself for some months entirely by short-term borrowing, as suggested by Chairman Eccles?

The last two questions present much the easier problems and may be considered first.

Action of the character proposed would be likely to cause a substantial decline in the market. The Treasury would, therefore, be open to a justifiable accusation of bad faith if it should undertake long-term financing while contemplating joining in such a recommendation.

Financing Treasury needs for the next few months exclusively by short-term issues would appear to present no special difficulties, except that most of the securities so sold would go into commercial banks and so would result in increasing bank deposits. Such an increase could be easily justified, however, if it were merely the first step in a program which would result in the long run in the sale of fewer, rather than more, securities to commercial banks.

It would seem, on the other hand, if you do not propose to concur with the Reserve Board in recommending an increase in reserve requirements, that there is no need for postponing long-term financing longer than might be indicated by the other factors in the situation.

The advisability of adopting Chairman Keeles' specific suggestions with respect to current financing operations, therefore, turns upon the broader question of the advisability or inadvisability of concurring with the Reserve Board in their proposal to increase reserve requirements.

## II. The Present Situation with Respect to Excess Reserves

Excess reserves amounted, on August 27, to \$5.0 billions. This is a decrease of \$1.9 billions since the all-time high reached on October 23, 1940. The factors accounting for this decrease are shown in the following table:

**Factors Accounting for Decrease in Excess  
Reserves, October 23, 1940, to August 27, 1941**

(In billions of dollars)

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**Factors absorbing excess reserves:**

Increase in money in circulation	1.7	
Increase in Treasury cash and deposits in the Federal Reserve Banks	.5	
Increase in required reserves	.8	
All other	<u>.4</u>	3.4

**Factors creating excess reserves:**

Increase in monetary gold stock	1.3	
All other	<u>.2</u>	1.5

Decrease in excess reserves		1.9
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It will be observed from the above table that total reserves declined during this period by only \$1.1 billions -- the remaining \$0.8 billions of the decline in excess reserves being caused by an increase in required reserves resulting from deposit expansion during the period.

About \$0.7 billions of the decrease in total reserves was caused by an increase in Treasury deposits and other more or less non-recurring factors. The remaining \$0.4 billions of the decrease was caused by the excess of the increase in money in circulation over the increase in monetary gold stock. The movements of these two factors are likely to dominate future movements in total reserves for some time to come.

As nearly as can be estimated -- barring changes in official policy, or the import of substantial amounts of gold from Russia -- total reserves appear likely to fluctuate within a relatively narrow range for the next year or so. This means

that any further substantial decrease in ~~excess~~ reserves is likely to come only from an increase in required reserves due to continued deposit expansion. Such a decrease in excess reserves would, of course, be inflationary, rather than deflationary, in its implications, as it would mean that some of the previously existing excess reserves had been transformed into deposits -- at a ratio of about \$5 of deposits to \$1 of excess reserves -- and had so moved one step further toward the spending stream.

III. Probable Consequences of an Increase in Reserve Requirements

The objective of raising reserve requirements is to assist in preventing inflation. The immediate effect of such an increase would be to reduce the available supply of bank credit and so to make banks less ready to lend and to purchase securities. It might also incline many of them to sell securities already held. This would be especially true as an increase in reserve requirements would hit the New York City banks the hardest and other banks are inclined to follow the lead of the New York City banks in handling their security portfolios. 1/

1/ The following table indicates the distribution by classes of cities of excess reserves on June 25, 1941, and the amounts to which they would be reduced if reserve requirements were increased to the present statutory limits:

	Actual Excess Reserves	Excess Reserves if Requirements Increased to Statutory Limits
(in millions of dollars)		
Central reserve cities	2,612	1,976
Reserve cities	1,750	1,398
Country banks	859	589
Total	5,221	4,058

The above table makes no allowance for withdrawals of inter-bank balances incident to increasing reserve requirements. The staff of the Board of Governors estimates that such withdrawals would not exceed \$75 millions.

(This footnote continued on next page)

Secretary Morgenthau - 7

An increase in reserve requirements would consequently increase interest rates and put down bond prices. This was agreed to by all members of the staff of the Reserve Board with whom the matter was discussed.

The extent of the increase in interest rates — and decreases in bond prices — would depend upon the character of the action taken and is difficult to predict. An increase in requirements to the present statutory limits, coupled with a definite assurance that no further increase was contemplated, might have very little market effect. A contemplated increase in requirements above the present statutory limit, however, would be bearish to an indeterminate degree depending upon its impact upon banker psychology. An increase in reserve requirements sufficient to reduce excess reserves below \$1 billion could very easily put new long-term borrowing on a 3 percent basis and put down the price of the new taxable 2-1/2's of 1956-58 by as much as 10 points. (This is about the same as the average decline in the prices of long-term Treasury bonds between the high reached in June 1939 and the low after the outbreak of the war.)

An increase in reserve requirements would also put down sharply the prices of all outstanding partially tax-exempt securities. It is true, of course, that such securities, because of their growing scarcity, would have a better chance of staging a recovery than would taxable securities, the supply of which is being constantly increased, but such a recovery might be a matter of years.

If reserve requirements were raised substantially, it would also probably be necessary to start new series of savings bonds at substantially higher rates than those now being offered and to refund into such new series many of the outstanding bonds which would be presented for cash redemption in order to take advantage of the higher rate. It might even be necessary (for reasons of public morale) to make the higher rates retroactive on savings bonds already sold.

(Footnote 1/ continued from preceding page)

If reserve requirements were increased to 25 percent above the present statutory maximum, the excess reserves of central reserve city banks would have been reduced as of June 25 to about \$712 millions and the aggregate reserve deficiency of all banks having reserve deficiencies would have been about \$600 millions.

Since June 25, the date to which the above figures apply, aggregate excess reserves of all member banks have decreased about \$241 millions.

Increasing the cost of borrowing to the Government would not in itself help solve the problem of inflation. It should be considered rather as a disadvantage of the proposed method of attack and should be weighed against its supposed advantages.

The first benefit in the fight against inflation likely to be derived from increasing reserve requirements is psychological. Increasing reserve requirements is a traditional method of combating the inflation incident to business booms and its use at the present juncture would probably be interpreted as a token of sincerity. The announcement of such a policy might tend, therefore, to dampen speculation in the commodity markets.

Such a psychological advantage would be short-lived, however, unless the increase in requirements had more fundamental consequences also. The primary consequence of the increase would be, as we have seen, a stiffening in interest rates. This stiffening would apply to all borrowers -- governmental and non-governmental, essential and non-essential alike. It would be effective in controlling prices, however, only as it actually reduced borrowing and hence spending. In order for the action to be effective, some borrowers would have to be squeezed out of the market. The Government and the defense industries would not be among the borrowers so squeezed out. They would have to pay whatever rate was necessary in order to obtain the requisite credit. This leads naturally to the question of whether an increase in rates is the best method of squeezing non-essential borrowers out of the market. This is the fundamental problem of the relative desirability of general vs. selective credit controls and will be considered in the next section.

#### IV. Relative Merit of General and Selective Credit Controls in the Present Situation

It is the purpose of all credit controls to reduce borrowing and hence spending, and so to restrain price increases judged to be undesirable. Credit controls may be classified as general and selective.

General credit controls operate by causing an all-around scarcity of lendable funds, thereby putting a general pressure on all borrowers to reduce their borrowings and hence their spendings. General credit controls to be effective must bring

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about an increase in the rate of interest, since it is through such an increase that general pressure is brought to bear upon borrowers. An increase in member bank reserve requirements is a general credit control. Open market operations (selling Government securities) by the Federal Reserve Banks constitute another.

Selective credit controls operate by wholly or partially shutting out a given class of borrowers from access to the existing supply of lendable funds. In this way, total borrowing -- and hence total spending -- is cut down without any necessity for a rise in the rate of interest. Selective credit controls already in operation consist of some limitation of stock market borrowing (by means of margin requirements) and some limitation of consumer credit. Other selective controls which might be availed of at the present time would be limitation of housing credit, restriction of new capital issues, and restriction of bank loans for other than national defense purposes.

The relative appropriateness of the application of general or selective credit controls to any situation showing evidences of incipient inflation, depends upon the character of the situation. If a more or less uniform contraction of borrowing all along the line is desired, general credit controls are more appropriate. If, on the other hand, it is desired to contract borrowing only in certain fields, selective controls are indicated. It is, of course, by no means barred that the appropriate remedy for some situations might be the application of both general and selective controls of varying degrees of intensity.

The present situation appears to call for the application of special and not general controls. The reasons for this conclusion are simple. The application of general controls would place a pressure (reflected by higher interest rates) upon borrowers all along the line. There are two very important classes of borrowers, however, who will not contract their borrowings a cent under this pressure, nor is it socially desirable that they should. These borrowers are the Federal Government and the national defense industries. Between them they will probably account during the current fiscal year for at least three-quarters of total borrowing, and they will have to pay whatever rate is necessary to secure the needed funds.

The pressure engendered by general credit controls, therefore, can be effective only with respect to the remaining

borrowers who together will probably account for not over one-quarter of total borrowing. Even these borrowers furthermore, under present insipient boom conditions, will be very hard to discourage by means of rate increases. The net effect of applying stringent general credit controls at the present time, therefore, would be to increase greatly the cost of borrowing to the Federal Government and to the national defense industries, in order to effect a relatively small contraction in borrowing for other purposes. Mild general credit controls would have a less drastic effect on interest rates, but by the same token, would be even less effective in combating inflation since it is only through the medium of an increase in interest rates that general credit controls are able to effect reductions in borrowing and spending.

Selective credit controls, on the other hand, may be concentrated solely on those areas of the economy where contraction is desired. Borrowing may be wholly or partially blocked out in these areas, thereby increasing the proportion of the total supply of funds available to the Government and the national defense industries. This seems more desirable than tightening credit conditions generally and forcing the Government and other defense borrowers to compete on a price basis for an expanding proportion of a limited supply of credit. The use of selective credit controls might be compared in this respect to the present policy of prohibiting the use of aluminum for pots and pans and so permitting its purchase for national defense purposes at a moderate price. The use of general credit controls could, by the same token, be compared with a policy of out-bidding the pot and pan industry for the available supply of aluminum. Either policy might be made to result in a diversion to defense needs of any given proportion of the total supply of aluminum -- but at very different costs.

#### V. Conclusions

It appears that selective, rather than general, credit controls should be relied upon for use in the present situation. Such controls will be more effective in checking inflation and may be applied without increasing the cost of borrowing to the Government and the defense industries.

Selective controls are already being applied to stock market loans and to consumer credit. Stock market loans at the present time constitute no problem. If at some time in the

future they should give signs of doing so, the existing controls should be tightened as much as necessary. The Reserve Board has just commenced the regulation of consumer credit. The initial regulations are very mild and will have to be tightened very considerably if the volume of such credit is to be substantially reduced.

Other fields in which selective credit controls may be necessary are housing, new capital issues, and bank loans for other than national defense purposes.

Housing credit could be reduced very substantially by the application of selective controls. At the present time the expansion of such credit is being actually promoted by advertising campaigns by the FHA and other agencies.

New capital issues do not present an important problem at the present time, but should be regulated by selective controls when and if they do.

Perhaps the most fruitful and immediate -- as well as the most complex -- field for the operation of selective credit controls is that of non-defense loans by banks. Member bank loans expanded by \$2.8 billions during the fiscal year 1941 -- a great deal of which must have been for non-defense purposes. If this expansion is in whole or part undesirable -- a necessary premise for the adoption of general credit controls -- some attempt should be made to get at it directly. The British have attempted to do this and their success in this regard has been an important factor in accounting for the low rate at which they have been able to finance the war. British banks have been instructed to relax their standards for defense borrowers, but to exercise rigid control over all credit for non-defense purposes. As a result, despite the increase in loans for defense purposes, total "Advances" of the London Clearing Banks have declined by about 216 millions since the beginning of the war, and an equal sum has consequently been placed at the disposal of the Government without an increase in bank deposits.

If, as suggested above, you should decide not to concur with the Reserve Board in a recommendation to raise reserve requirements, there would appear to be no necessity to defer long-term financing longer than might be indicated by factors in the situation other than the proposed increase in reserve requirements.

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August 22, 1941.

MEMORANDUM

TO: Secretary Morgenthau  
FROM: Mr. Gaston

Marriner Eccles called me today to say that he was leaving tonight to be gone for three or four weeks and he would like to give us his thoughts on September financing, if there should be any, a subject on which he had not had an opportunity to talk to the Secretary although he had mentioned it briefly to Mr. Bell.

Mr. Eccles hopes there will be no long term securities offered in September or at any time up to December, but that such new money as we may require may be procured by means of bills. His reason was that the market today is based on a large volume of excess reserves. There are few long term taxable bonds outstanding. The two issues out are both selling on a two per cent yield basis. If there should be any new long term financing in September it would naturally be priced at near today's market. This would mean in effect freezing of the present situation. By that he meant that our hands would be tied as to any action to change reserve requirements. We have not yet used the present power to increase reserves, which amounts to about a billion and a quarter. He thinks Federal Reserve should consider with the Treasury an increase in the reserve requirements up to the limit of existing power. Not only should this be done before any new long term securities are issued, but he thinks that the Treasury and the Federal Reserve should join in saying that it seems advisable to get further powers for increasing reserve requirements and that both these things should be done so that the market can absorb their effect before any new long term securities are put out. Otherwise he thinks the Administration, including the Federal Reserve as well as the Treasury, would be open to charges of bad faith.

Copy to:  
Mr. D. W. Bell

BOARD OF GOVERNORS  
OF THE  
FEDERAL RESERVE SYSTEM

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Office Correspondence

Date September 2, 1941

Mr. George Haas

Subject: \_\_\_\_\_

Mr. E. A. Goldenweiser

This memorandum is for the purpose of raising the question of the advisability of deferring long-term Treasury financing until after a decision has been reached in the matter of raising member bank reserve requirements.

In the light of developments in the last few months, it is clear that, from the monetary point of view, it would be in the public interest at this time to raise reserve requirements of member banks to the extent authorized by law. This would fix the requirements at double the ratios stated in the law and would reduce excess reserves by about \$1.25 billion to about \$3.8 billion. Consideration should also be given to the advisability of seeking additional authority over reserves to be available for use when the occasion arises.

An increase in reserve requirements would be in line with other measures undertaken by the Government to prevent inflation, such as, for example, the request for authority to control prices and the adoption of restraints on installment purchases. An increase in bank reserve requirements would reinforce the public's confidence that the Government is determined to control inflation. Such an assurance to the public would in itself reduce the danger of inflation which is accentuated by a widespread tendency to buy goods in excess of needs "before prices go up".

An increase in reserve requirements would also diminish the pressure on banks to find outlets for their funds and would strongly reinforce the policy pursued by the Treasury to place its issues with purchasers other than banks in order to tap existing funds rather than to create new ones. So long as the banks have unlimited reserves it will be difficult to limit their purchases of United States Government obligations. During the fiscal year 1941 banks absorbed an amount equal to nearly all the open-market securities offered by the Treasury. If securities issued are not available to banks, they will be in a position to buy outstanding securities from other investors who will, in turn, buy the new issues. The banks will also be under pressure to extend credit in other directions.

Selective credit controls, such as regulation of instalment credit, have a place in the program. They cannot, however, take the place of general controls, for several reasons. So long as banks have unlimited funds and there is active demand for credit, the banks will find outlets for their funds. If one field is restricted, they will move into another field. No matter what kinds of loans or investments banks make, there is an expansion of deposits available for spending by the public. Also the problems of selective controls are new, complex, and there has been little experience in handling them. They also raise problems of discrimination. Selective controls are useful in directing the flow of credit out of undesirable into desirable channels, but they are not an adequate means of restricting the total growth of bank credit and deposits.

In connection with the problem of reserve requirements, it is recognized that in present circumstances coordination of all financial policies is essential to the public interest and that nothing should be done that would conflict with the Government's defense effort. Agreement on a policy with regard to reserves is, therefore, necessary before action is taken.

In this connection the question arises whether it would be feasible for the Treasury to defer announcement of any contemplated long-term new financing until, say, October 15, when the question of increasing reserve requirements will have been explored. It would not seem desirable to issue a long-term security in September, and immediately after that to raise reserve requirements. In view of the volume of available funds in the hands of banks and other investors, raising requirements to the limit authorized by law should not result in any material change in money rates, though there may be some temporary reaction in the market. In that case, the purchasers of the new issue may feel that it was not fair of the Treasury to sell the bonds under now prevailing market conditions without letting the public know that action on reserves was under consideration. It would seem to be far better to have the question of the course of action to be pursued with respect to reserve requirements decided before the Treasury makes another long-time offering to the public.

The Treasury and the Federal Reserve System are in a position to establish and maintain any rate on Treasury borrowing that they may determine as the most desirable, and it would be the System's duty, when the decision has been made, to support the rate selected. But it is a legitimate question whether a slightly higher cost for borrowed money would not, in the long run, be cheaper for the Government, which is the largest purchaser, as well as more consistent with the public interest than a slightly lower cost achieved at the risk of a general rise in

prices of defense and other commodities. Besides, an interest rate declining constantly to lower and lower levels, which is the tendency under present conditions, raises many far-reaching problems for the economy as a whole.

Sales of savings bonds and tax-anticipation certificates have exceeded expectations, and it is believed that the Treasury has ample funds with which to meet its current requirements for some time to come, so that it would be entirely practicable to defer new financing to the middle of October.

*E. A. Goldenstein*

The Role of the Banks in Treasury Financing,  
in Relation to Problems of Credit Control

In assisting the Treasury to raise whatever funds are required, supplementary to tax revenues, to place purchasing power in the hands of the Government during the next few years of economic warfare, the banks have two functions to perform. One of these functions is that of dealers in outstanding issues. The other is absorption of part of the increasing Government debt in their investment portfolios.

Little discussion of the dealer function is required. No matter what credit policies are adopted, the Government can arrange to have this function adequately performed. A brief analysis of this question is given in an appendix.

The basic issue at the present time, both for Treasury financing and for credit control, is this: how seriously should the Government take the conventionally respectable idea that participation of the banks in Government financing should be held down to a minimum in time of war or economic war?

This issue may be expressed in three more or less equivalent forms. Should the growth of bank assets and deposits be held down? Should interest rates be increased? Should some attempt be made to reduce the idle funds of investors? (It will be shown below that actually it will be impossible to reduce idle funds — apart from their activation by an inflationary development — except by a complete immediate curtailment of bank credit. Such dramatic action is not proposed or considered in this memorandum.)

Arguments on the negative side are very powerful. Strong action to hold down the growth of bank assets might mean a breakdown of the defense effort through "unnecessary" interference from the side of finance. It would involve a collapse in market values of the present assets of banks and other institutions. These and other arguments are outlined in the first main section of this memorandum.

On the other side there are arguments for early and forceful action to hold the participation of the banks in Government financing to an absolute minimum. These arguments are logically coherent, but it is not likely that they will find general acceptance. They are presented in the second section of this memorandum.

Some sort of a compromise solution is possible. Essential elements of this program would include: (1) stability of interest rates; (2) utilization of all possible devices short of restriction of excess banking reserves to test out and stimulate the absorptive powers of the non-bank investment market; (3) full exploitation of taxation and selective credit controls to moderate the force of consumer demands. The idea of decisive action to prevent inflation through credit controls would be abandoned, the banks would be allowed to contribute as fully as necessary to the easy success of Treasury financing in doing its part in "winning the economic war", and the Government would hope to avoid the choice between inflation and rigorous regulation of consumption by carrying out a broad program of fiscal and other controls.

The present economic situation is in many ways very different from that to which we have become habituated in the past several years. There is now only a small and gradually disappearing margin of overcapacity in basic manufacturing, transportation and electric power industries. We are assured of a powerful stream of effective purchasing demand for some time to come. So long as the Government's expenditures under the defense program continue to increase, and possibly for a while thereafter, the Federal Reserve System need not have the slightest fears that any action of credit control will be followed by a serious recession in business activity. Although the conditions which limit Federal Reserve policy have been tightened by the necessity of "Winning the war", they have been relaxed in another direction as a result of this certainty of prosperity.

Acceptance of Government controls of economic life during a period of economic warfare is much more general now than twenty-five years ago. In the first World War our Government imposed no controls until 1917; under the stimulus of a booming export trade with the Allies and as a result of other events in the world at war, the wholesale price index had already risen by 75 per cent and the cost of living by 25 per cent. Earlier recognition of the problem of preventing inflation raises the hope that we may avoid inflation this time. (A doubling-and-a-half of the price level, such as occurred between 1915 and 1920, must be regarded as true inflation.) However, there is no more intention now than there was in 1915, 1916, or even 1917 and the first half of 1918, of imposing rigorous controls upon consumers

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buying. <sup>1/</sup> Beyond this, there is one factor now present, not present twenty-five years ago, which seriously threatens the success of price-level stabilization. This is unprecedented cash liquidity in the banking system and among savers and investors.

Major uncertainties in the present situation, which make decisions on credit policy difficult, are (1) the eventual size and timing of defense expenditures and (2) the amount and distribution of slack still remaining in the country's productive capacity. These two uncertainties are related since capacity is not absolute but is capable of growth at a limited rate. It is only natural that these uncertainties will continue to be resolved in favor of decisions to avoid far-reaching controls -- steep consumption taxes and price-fixing and rationing of consumers' goods -- at least until some measure of true inflation of the cost of living has already taken place. Such forms of control are in themselves still abhorrent to a democracy. Once imposed, their removal after the war would have serious economic repercussions unless performed with care.

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<sup>1/</sup> "Price fixing" on consumer goods was limited to the regulation of processors' and distributors' margins on food and coal. This was of limited effectiveness because it was not possible to control the farm prices of feedstuffs. Sugar was the only consumers' commodity subjected to compulsory rationing. Only by the summer of 1918 were plans being made to fix the prices to consumers of some other articles such as shoes.

Arguments against preventing banks from greatly increasing their holdings of Government securities

(1) The most powerful argument is the fear that it would prove quite impossible to dispose of the Treasury's output of new securities without calling upon the banks to absorb a considerable part. This argument is somewhat weakened if it is proposed only to reduce excess reserves, say to \$2,000,000,000; in that case this problem would not be pressing at first. Within a fairly limited time, however, it would assert itself, and any plans made now must look ahead for several years.

(2) The next most powerful argument is that a rise in long-term interest rates would result in a tremendous drop of market values of bonds now held by the banking system and other institutions. Incidentally, while the question at issue is whether or not a growth in bank holdings ought to be substantially prevented, this could not be accomplished without an elimination or substantial reduction of excess reserves. (For even if banks were flatly prohibited from subscribing to new issues they could buy up outstanding securities.) There is difference of opinion about the immediate effect on long-term interest rates of the imposition of a "ceiling" plan cutting excess reserves say to one-third their present volume. It seems evident, however, that long-term interest rates would seek a higher level as the remaining excess reserves were absorbed and some idle deposits of investors were drawn into the Treasury either by taxation or borrowing, even though no net decline in idle funds would occur. Such an eventual rise of long-term rates might or might not be discounted by the market from the outset.

However, a thoroughgoing program for the prevention of such further growth in bank investments would include action by the Treasury to insure that this inevitable rise in interest rates took place immediately and ease for all. This could be accomplished very effectively by the Treasury offering long-term and intermediate securities on tap in unlimited quantities at par with a 4-5 per cent range of rates. (This is approximately 1 per cent above the presently anticipated yields on fully taxable bonds.) Such action, in conjunction with a cut in excess reserves, would lead to an immediate and fairly precise readjustment of bond prices. The forced rise in yields on the new tap issues, and therefore on all issues competing with them, would be greater than any foreseeable future rise flowing only from the cut in excess reserves. It is unlikely that the tap issues would be unacceptable to investors, that these issues would go to a discount, or that the general level of yields would rise beyond the rate structure envisaged by the coupons on these issues. Subsequent fluctuations of bond prices would be much smaller than those we have become accustomed to.

Such action to force an immediate readjustment of bond prices and yields has much to commend it as part of a realistic program of restricting bank investments. But the prospect of a 15-point decline in market values of portfolio bonds would be alarming both to bankers and the Government.

(3) The rise in interest income accompanying such a shift in yields would be of no great advantage to the banks if they were to be substantially deprived of the opportunity to buy the net high-rate bonds.

However, loan rates would rise, and as loans turned over the banks' gross earnings would increase.

From the Treasury's point of view, however, the higher rates would appear very costly. On thirty or forty billion dollars of new debt, a difference of 1 per cent in rate would enlarge the annual interest charges by three or four hundred million dollars. Added to this there would be the extra charges on issues to refund maturities during the years the high rates remained in effect.

(4) Finally, arguments may be advanced on economic grounds: the rise in rates would accentuate the unequal distribution of national income; it would be injurious to commerce and industry and perhaps even to the defense effort since it would inhibit expansion of industrial and housing capacity; higher rates would be "uneconomic" in these modern days when industrial productivity has reduced the demand for capital far below the supply.

These arguments, unlike the others, may be briefly dismissed. They indicate too much habituation to the economic climate of recent years, or they assume, fallaciously, that the higher level case imposed would be permanent. Diversion of income from consumers to investors, undesirable in normal times, will be desirable in "war-time" (provided that the extra income paid to investors can be recaptured, by taxation preferably, or at least by borrowing) because a temporary reduction in consumption will be necessary. A reduction in new housing construction will be particularly desirable at a time when durable materials and labor will be scarce. Industrial expansion, unlike

housing construction, is almost totally insensitive to interest rate changes; and profits (even after high corporation taxes), supplemented by moderate use of the new-security markets and of bank loans so long as they remain available, and further supplemented by direct Government financing, will provide sufficient funds for all expansion expenditures which prove necessary for defense or otherwise permissible. Finally, the opportunity of once again lowering interest rates and of making loan funds freely available would be of positive value in combatting post-war recession.

In summary, three powerful obstacles oppose any through-going effort at present to restrict the expansion of bank assets and deposits: fear of a breakdown of Treasury finance, fear of a great drop in institutional asset values, and dislike of an increase in the Treasury's costs of financing. Moreover, these obstacles will persist. The second and third may come to seem less important if inflation of the cost of living gets under way, but the fear of a breakdown in Treasury finance will be greater, not less, if restriction of the credit base is proposed later, at a time when the Treasury will have become thoroughly habituated to relying on the banks for a substantial part of its new money.

Arguments in favor of preventing banks from greatly increasing their holdings of Government securities.

To make a case against the powerful arguments which have just been considered, it is necessary first to establish a reasonable presumption that the economic war can be financed without the assistance of the banks, second to bring forward positive arguments for the necessity of limiting bank expansion, and third to show that other objections are immaterial.

The conclusions which can be reached are by no means irrefutable. They come out something like this.

(1) Treasury financing can get along without such assistance from the banks, if taxes are raised sufficiently and are supplemented by forced loans in the event that the defense program is materially increased beyond present expectations, if the outlook for future interest rates is clarified and the Government's determination to prevent inflation is made obvious, if a rise in interest rates is not only permitted but authorized by the Treasury, and if a "ceiling" plan of bank reserves is adopted coupled with a plan for the Federal Reserve Banks to absorb temporary or persistent Treasury shortages without at the same time supplying the member banks with an additional base for multiple deposit expansion. For a number of reasons, if Treasury financing is ever to get along without a great deal of assistance from the banks during this period of economic war, the measures which would make this possible must be undertaken very soon. The outlook for future interest rates will remain hazy and there will be recurring expectations of inflation so long as credit restriction remains a future possibility and not a present fact. This means that

investors will continue to shy away from the bond market. On the other hand, the Treasury's plans for future interest rates will not be easily altered once they are made, and they would undoubtedly have to be altered at a time of abstaining from bank finance. The total amounts to be raised by taxation as over against borrowing can be adjusted only annually, and for a period lying several months in the future. No sudden increase in taxation will be possible at the moment that credit restriction becomes desirable.

(2) If it is assumed that inflation of the cost of living and of real estate values comparable with that which occurred in the last war must be prevented this time, and if it is believed that this can be done with the aid of monetary controls, preparation must be made now to utilize monetary controls at the appropriate moment. Fiscal arrangements must help to keep consumer demand in line with available supplies of basic commodities and Government policy must continue to be directed at increasing supplies and seeing that they are fairly distributed among the defense and non-defense industries at reasonable prices. But rigorous regulation of the consumer himself as in Germany (or of the purchaser of real estate) is neither desirable nor likely to be adopted in time. Therefore, almost assuredly, measures will eventually have to be taken, and perhaps within a year, that will sharply reduce the availability of money to consumers and speculators and to business firms and corporations trading in inventories, at the moment when as a result of pressure from effective consumer demand the vicious cycle of price-cost-price inflation begins. Unfortunately, because of the unprecedented cash liquidity of individuals (as well as banks),

this action is far from certain to accomplish its purpose. Merely to close the private loan market at that future moment will not necessarily suffice, for idle funds will pour into the real estate market, the stock market, and -- so far as possible -- into purchases of consumption goods. The most that can be said is that the chances of success will be greater the more nearly idle funds have been held to their present level instead of being allowed to increase at a rapid rate. With the help of stock market regulation, perhaps the psychological shock of a complete closing of the loan market will be enough to precipitate a temporary reversal of the boom psychology, despite the tremendous pressure of consumer demands. But if idle funds are allowed to continue to pile up before this time comes, and it is hard to see how this can be avoided, the chances of success will be negligible.

Estimates are given below which suggest that demand deposits and currency now held for investment purposes by individuals or hoarded amount to something like 17 billion dollars, as compared with perhaps 7 or 8 billions in 1929. It is further suggested that if stability of the price level can be maintained during the next two years without restricting bank expansion, and if in fact the Treasury borrows \$15 billions from the banks out of a potential two-year total financing of close to \$30 billions, <sup>1/</sup> the growth of deposits in excess of the requirements of governments, corporations and consumers might amount to another \$17 billion, bringing the total of individuals' idle funds to well over \$30 billions!

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<sup>1/</sup> This is on an assumption that something happens to step up defense outlays from a now probable \$30 billions to \$40 billions during the calendar years 1941 and 1942.

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A very early restriction of bank expansion — as for example by the use of the ceiling reserve plan with excess reserves cut to a third — is therefore necessary if any reliance at all is to be placed on the power of closing the private loan market completely. But the virtue of this action now would not be solely in its aspect of preparation for other action later. In a much more concrete and certain way it would help to maintain the conditions that would make the later action never necessary. The Treasury in agreeing to this program would commit itself to an extremely heavy schedule of taxes and forced loans, for only in this way could it get along without much help from the banks. Returning to the figures cited in the preceding paragraph, if the Treasury were to expect only \$5 instead of \$15 billions from the banks out of prospective two-year borrowing requirements of say \$25 billions, while other institutional sources might be counted on for \$5 billions at the most, it would have to manage to get \$19 billions instead of \$9 from individuals. In no conceivable way could it get such a sum within a two-year period without resorting to steep income and payroll taxes and forced loans. And nothing could more satisfactorily perform the task of transferring purchasing power from consumers to the Government in a way that would avoid price inflation.

The central argument for restricting bank expansion therefore has two facets. On the one hand this policy would diminish the potential further growth of idle funds (but not stop it); on the other hand it would necessitate stiff taxation and forced loans which offer the

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only sure safeguard against inflation -- short of completely effective price-fixing and rationing -- if the defense program is to be enlarged beyond present expectations.

If the defense program does not exceed the proportions that can now be envisaged -- if defense outlays in the calendar years 1941 and 1942 are not to exceed say \$30 billions, and financing requirements in the same period are not to exceed say \$21 billions according to tax plans now expected -- a more rigorous taxation scheme may not be required. But in this case the higher interest rates, and above all the fixed interest rates, which the plan outlined on pages 5 and 6 would bring, would certainly be of assistance in disposing of savings bonds and long-term issues.

(3) If inflation is almost inevitable in the absence of either rigorous control of the consumer or foresighted monetary controls, and if immediate monetary controls can remove the necessity for future controls by persuading consumers to part with their money or by causing the Treasury to force them to part with it, then it is easily worth the cost to the Treasury of an extra interest burden of a few hundred million dollars a year to take its share of leadership in planning such monetary controls.

The temporary check to the bookkeepers of bond values, implicit in any plan which raises interest rates, is of no real consequence. There is no need for any bank to sell bonds before maturity, much less for any bank to fail as a result of doing so. New high-rate bonds will be made more not less attractive since there will be an

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excellent chance of their appreciating in the years immediately following the war when interest rates are lowered.

It will be observed that these conclusions have been based on a series of three assumptions; first, that the industrial and fiscal controls likely to be undertaken in the absence of immediate credit control are not likely to prevent the emergence of the vicious cycle of inflation; second, that the inflationary cycle when it emerges may possibly be killed by closing the private loan market, but certainly not if investors' idle funds have continued to increase at a rapid rate; third, that it is politically and administratively feasible to undertake the preliminary credit controls and the additional fiscal planning which will be necessitated (and which, in fact, will be the most valuable product of the credit controls). Without arguing these assumptions, the reasoning underlying the conclusions can be developed with the help of some figures.

The two charts attached show the estimated ownership of deposits and currency over the past decade. These estimates are fairly accurate for the years 1934-1938, somewhat less so for earlier and later years. In the second chart the cash of "individuals" (intended to include in an approximate way the cash of unincorporated businesses) is broken down into (1) savings deposits, (2) "consumption cash" arbitrarily taken equal to half a month's "national income payments", and (3) other cash. Changes in the last category roughly represent changes in reserve cash of investors and boards. As an index of hoards or "idle money" in

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the sense of unaturally large investment reserves, its variations from average probably understates the real situation by \$2 or \$3 billion in 1931 and 1932 and may overstate it by \$1 or \$2 billion in recent years. As of the end of 1935 it is indicated that investment-and-idle money was about \$1 billion greater than in 1929; by the end of 1940 the excess was \$9-1/2 billions.

The table brings together a number of significant facts relating to the distribution of Government debt and of cash holdings since the end of 1935, along with four sets of hypothetical statements for the years 1941-42. The first two of these represent developments with the defense program and tax structure approximately as assumed in Mr. Edmiston's memorandum of March 24, 1941; the first column assumes adoption of the program on pages 5 and 6 of this memorandum and no rise in the price level, while the second assumes a 20 per cent rise in prices over the two years. Similarly, the second of the last pair of columns assumes a 40 per cent price rise under a considerably enlarged defense program. As will be shown later, the construction of a table like this for future periods involves the hidden assumption that the amount of current saving (or increases in individual assets) implied by the figures is consistent with the assumptions made about national income and the price level, and measures taken to enforce saving.

One more column might have been added to illustrate the example that was cited on page 11 above. This example combined the assumption as to price level of column A-2 with the assumption as to

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distribution of Government debt of column B-2. The appropriate figures may be derived by adding \$10 billion to lines 2, 3, 5, and 13 of column A-2, and deducting \$10 billion from line 14, the other figures in that column remaining unchanged.

A brief comment may be made upon each of the main items. In 1941 and 1942, Government financing with the banks and public will be at a rate from 10 to 15 times the average rate of the last five years. Commercial bank holdings will increase at least twice as fast, perhaps 4 or 6 times as fast. The growth of deposits and currency outstanding will exceed the growth of commercial bank investments as in past years, though this will now be due more to expansion of loans than to gold inflows. Holdings of "nonindividuals" may either increase or decrease, depending most importantly upon the effect of price changes upon non-financial business holdings. The figures for the latter understate the changes in total business cash and equivalent (from an estimated level of about \$13 billion at the end of last year) because it has been assumed that \$2 billion of a special offering of Government securities will be purchased by corporations.

Under any circumstances short of an actual decline in bank assets, it seems certain that individuals' cash holdings will increase. Moreover, the rate of increase will be greater than even in 1919 and 1940. The same will be true of the growth of individuals' investment-and-idle cash, despite the probably more rapid increase in savings deposits and in cash needed for current income-and-consumption turnover.

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The amounts of Government securities to be absorbed by individuals in 1941 and 1942 under the various assumptions, as shown in the last line of the table, are derived by deducting the assumed increases in bank and other institution holdings from the figures in line 1. In every case these amounts are well-nigh astronomical as compared with individuals' net absorption of Government securities in recent years. Individuals have been buying several hundred millions a year of savings bonds, and disposing of other issues on balance. What is required, then, is an increase in the absorption of savings bonds and a reversal of the aggregate position of individuals toward the marketable issues. The Treasury hopes that the new savings bonds will bring in from \$2-1/2 to \$4 billions a year. If other issues can be sold to the noninstitutional public in annual volume of say \$2 or \$3 billions a year, it would be possible to fulfill the conditions of three of the hypothetical columns. That is, with a defense program not exceeding \$21 billions in 1941-1942 (or \$15 billions in fiscal 1942) it should be possible to get along without selling more than \$5 billions to the commercial banks (column A-1), and if there was no restriction of bank credit the financing problem would be still easier (column B-1). Likewise if there is a substantial expansion in the defense program as assumed in column B-2 the financing problem will not be too difficult, if \$15 out of \$29 billions to be borrowed are obtained from the banks. In each of these cases forced loans would presumably not be necessary during the period considered, but it would be a great help in obtaining the marginal \$1 or \$2 billions to be able to offer higher interest rates than now

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prevail and to be able to assure investors that the rates offered would be the maximum ever to be available. This will be particularly important if a positive effort to limit bank expansion is undertaken through an immediate cut in excess reserves.

If the defense effort is yet to be enlarged again in the near future, to an expenditure total of say \$20 billion in fiscal 1942, a thoroughgoing and successful program to prevent inflation by reducing excess reserves and restricting bank expansion would require the sale of perhaps \$19 billion of securities to individuals <sup>1/</sup>, or else equivalent measures of extra taxation and forced lending. This is the example shown in column A-2, and already mentioned on page 12 above. To repeat what was said there, nothing could accomplish the purpose of preventing inflation more satisfactorily than this kind of a fiscal program to keep Government debt out of the banks.

Are the hypothetical figures for "individuals' holdings" in this table, especially in column A-1 (presently estimated defense program with control of bank expansion), consistent with other applicable data such as the estimated average national income of about \$90 billion over the two-year period ahead? And can figures arrived at as these are by a calculation of residuals be taken to represent a probable or possible situation? The estimation of change in total holdings of cash offers no difficulty, once assumptions have been made as to the amount of change in bank assets. The figures for other holdings

<sup>1/</sup> The taxes assumed in deriving this figure already include some additional levies to become effective immediately during the fiscal year 1943.

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may be somewhat in error, but they reflect so far as can be estimated the probable desires of the various groups to hold cash; consideration is also given to such factors as volume of capital expenditures or investments and availability of funds from earnings or borrowings. There is nothing inherent in a great increase in bank deposits which automatically forces anyone or any group to hold its proportionate share of the increase. But can similar reasons be offered to explain why individuals are likely to hold just the amount of cash that the residual calculation has allotted to them? Is there not something paradoxical in the expectation that individual cash holdings will increase so sharply while at the same time the assumption is being made that individuals will absorb a very large volume of new security offerings?

This question is posed in a most violent way by the figures in column A-2, where individuals are expected to absorb a total of \$30 billion of cash and Government securities (or perhaps submit to heavy taxation), and in column B-2, where they are expected to absorb \$24.5 billion (the total of figures in fifth and bottom lines). Column A-2 offers the lesser difficulty, because it was assumed in this case that price stabilization succeeds. It succeeds only through very drastic taxation, as a substitute for part of the assumed borrowing, or through forced loans. The very same thing that maintains price stability -- and thereby justifies the estimates made for non-individuals and the whole residual calculation -- will force individuals

to absorb Government debt (or be further taxed) on top of a rather large increase in their aggregate cash holdings, especially in those held idle by investors or as hoards.

The case of column B-2 is somewhat different. The assumptions here are: no restriction of bank expansion, and a 40 percent price rise by the end of 1942; national income will therefore average about \$110 billion. The greater rise in national money income calls for a considerable increase in cash turning over from week to week, and this increase in individuals' average holdings will no doubt be in the nature of an addition to whatever other increases in individuals' assets might occur as the result of what is ordinarily called saving. There will also be a somewhat greater than ordinary increase in savings deposits, and a very considerable increase in business cash holdings, permitted by larger profits and required by the higher price level of commodities and labor. Thus the final residual of "individuals' investment and idle cash" (8.5) when added to the assumed absorption of Government securities by individuals (9.0) adds to a total no larger than that assumed in column A-1 (6.9 + 11.0). This in itself does not necessarily validate the B-2 estimates, even if the A-1 estimates are acceptable. Despite the probably higher level of individual savings in case B-2, it is probable that under boom conditions a part of these savings would be placed in real estate and stocks rather than in cash and bonds. If, in the final analysis, it should be decided that the residual estimate in column B-2 does not correspond to the probable facts of the situation as defined, then the whole

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situation must be redefined. It might be that with Government expenditures as large as here assumed, and with no restriction on bank expansion, that the price increase would be even greater, that business cash would be built up still more, and that a revised residual calculation of individuals' holdings would finally check with a direct and independent estimate.

Finally, we return to the case presented in column A-1 (presently estimated defense program with control of bank expansion). The residual calculation of increase in total individual holdings (including savings deposits and turnover cash) is \$11 billion, and the assumption of individuals' absorption of Government securities is another \$11 billion for the two-year period. Can we conclude, on independent grounds, that these are reasonable figures and that the basic assumption of avoidance of price inflation is therefore validated?

Let us first compare the yearly average total increase of cash and Government debt holdings of individuals, \$11 billion, with the corresponding average for 1936-1940, \$3 billion a year. This is not encouraging at first sight. On the other hand, the rate of individuals' saving (abstention from consumption or increase in net worth), will average considerably higher in 1941-1942 than in 1935-1940; some estimates would seem to place the probable difference as high as \$4 or \$5 billions. New savings placed in life insurance will apparently continue at much the same rate as in the earlier period. In the earlier period the net aggregate change in individuals' assets

other than cash, Government securities, and insurance appears to have been rather small and perhaps negative, according to the rough estimates that are available. In the earlier part of the period some net saving was probably applied to repayment of debts; in the latter part some may have gone into home equities; individuals appear to have been net sellers of private securities on balance. If we can assume that the part of new saving going into these and other miscellaneous forms will continue to be small or even negative on balance in the coming period -- and the restriction of credit will help by reducing residential construction activity -- we still seem to be about \$3 or \$4 billions a year short of the necessary \$11 billions. The following alternative conclusions are indicated: either the additional necessary new saving by individuals can be induced by stabilizing and increasing interest rates, with the help also of an intensive promotion campaign for savings bonds, or the original conclusion that the price level could be stabilized without more drastic increases in taxation appears to be invalidated.

One other angle of the problem deserves attention. How are the changes in cash holdings and in bond holdings likely to be distributed as between the rich and the less well-to-do? It is probable that the major part of presently existing "investment and idle funds", perhaps two-thirds of it or more at a guess, belongs to the group who reported taxable incomes over \$5,000 in 1936 and 1937 and who had an aggregate taxable income of about \$9 billion a year out of national income payments to individuals of about

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\$70 billion in these years. Much of the aggregate net saving of recent years that went into cash and savings bonds was probably performed by these people, but it does not seem likely that even with their total incomes after taxes reaching say \$12 billion a year they are likely to save more than a half, let us say, of the required \$11 billions a year. Thus, not only must total new saving of individuals be increased, but new saving of the large lower-income group must especially be stimulated. The lower group can be expected to "save" -- i.e., add to its holdings -- most of the \$1/2 billion a year increase in active consumption cash. It will also acquire a minor part of the added savings deposits and idle cash. Beyond this, it must be stimulated or if necessary forced to lend to the Government, or be taxed, if we are to pass through 1942 without the beginnings of price inflation.

In conclusion, the one point which deserves most emphasis in a discussion of general credit restriction is that the chief virtue of such a policy lies in the Treasury's adherence to it, implying a determination to cut down, by taxation, voluntary saving or forced saving, the effective consumer demands which compete in time of economic war with the Government's own demands for relatively scarce supplies of labor and goods.

AppendixThe Banks as Dealers in Government Securities

The attractiveness of Government securities as investments depends not only on the perfect certainty of receiving interest and principal payments when due, but also on their liquidity -- the possibility of disposing of them at any time at a fair price.

Government securities may be either negotiable or non-negotiable. Liquidity is given non-negotiable securities -- such as the outstanding savings bonds and the proposed new issues of savings bonds -- by the Government's promise to redeem on demand or after a specified notice period. The Treasury would find it undesirable to have a very large part of its debt redeemable upon notice or demand. It will therefore continue to issue marketable securities, even if it adopts the tap method of sale for some of them.

Marketable securities must have a market. The banks are now an indispensable part of this market. Individual transactions in Government securities frequently reach a much larger size than is ever reached by individual transactions in stocks on the exchanges, or even by "secondary distributions" of stock holdings through syndicates of underwriters and dealers. The half-dozen non-bank dealers in Government securities would provide, by themselves, an utterly inadequate market. Of course, many of the large sales come from banks. But even if we imagine the banks somehow forced to hold

their Government securities to maturity, never selling any part of their holdings, the non-bank dealers would provide an inadequate market for other offerings.

There are three ways in which this inadequate market can be supplemented. One is the present way, whereby banks in general buy and sell and some banks in particular operate special trading departments. So long as other arrangements are not made to provide an adequate market, it would be entirely inadvisable to prevent banks from buying and selling any Government securities that are to be otherwise negotiable. Even if excess reserves were greatly reduced or eliminated the banks could be freely allowed to carry out this function of acting as dealers. The Federal Reserve System might provide special discount facilities, at a low rate, to finance dealer transactions on a turnover basis.

A second way of providing an adequate market is to let both the member banks and the Federal Reserve Banks deal in securities. The Federal Reserve Banks might enter the market purely as broker-dealers, accepting the bids and offers of others, or they might operate as traders initiating transactions. The more they operated as traders the more nearly the market could be pegged. It may be desirable to peg the market during a period in which a vast quantity of securities are to be sold. One usual objection to the Federal Reserve Banks' operating in this way is that their operations would affect the reserve position of the member banks.

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This objection may lose its force in the present situation. On the one hand, if a program of credit restriction is adopted it might include the "ceiling" reserve plan, under which multiple expansion on newly acquired reserves is not possible. Not only could the Reserve System safely peg the market; it could safely stand ready to absorb any persistent shortage of funds. This would set at rest fears that credit restriction might cause a real breakdown in Treasury finances. On the other hand, if a program of credit restriction is not adopted, changes in excess reserves due to Federal Reserve trading operations would be of little consequence.

The third way of providing an adequate market is for the Federal Reserve Banks to supplant the member banks entirely. In this case it would be possible to prohibit banks from purchasing any Government securities during the emergency and to prohibit them from ever selling Government securities before maturity. But no purpose would be served by this drastic innovation that could not be well served in some other way.

Estimated and Hypothetical Changes in Cash Holdings, 1936-1942  
 (excluding deposits at Federal Reserve Banks and Interbank Deposits)  
 And Hypothetical Assumt and Distribution of Increase in Government Debt

(in billions of dollars)

	: Hypothetical, End 1940-End 1942			
	: Estimated Changes :		: 2 years	
	End 1939-End 1938	End 1938-End 1940	exp. = 30	exp. = 40
Gov't public securities, incl. savings bonds 1/	+5.9	+4.2	+21.0	+29.0
Gov't securities of commercial banks	+1.4	+2.7	+9.0	+5.0
Total holdings of deposits and currency 2/	+7.1	+10.7	+30.5	+34.5
Holdings of "individuals"	+2.2	+2.8	-0.5	-0.5
Holdings of "individuals"	+5.1	+7.9	+31.0	+35.0
Holdings of "nonindividuals":				
U. S. Government	-	-0.2	+0.8	+0.8
Other public bodies	+0.4	+0.4	+0.1	+0.1
Foreigners	+0.5	+0.7	-0.4	-0.3
Financial corps. and bank trust depts. 3/	+0.2	+0.5	-0.4	-0.5
Nonfinancial business, corp. and other 5/	+3.1	+3.4	-0.7	-0.7
Holdings of "individuals":				
Savings deposits	+2.1	+1.9	+3.1	+3.1
Currency and demand deposits held for consumption 2/	+0.2	+0.4	+1.0	+2.0
Demand deposits and currency held for investment or hoarded 6/	+2.8	+5.5	+5.9	+7.8
Gov't securities to be absorbed by "individuals" if additional taxies were not imposed 7/	+1.1	+0.7	+11.0	+9.0

Note: It is assumed that national income at present prices, reaches \$100 billion by the end of 1940. Under A-1 and A-2 it is assumed there is no price rise, under B-1 20 percent, under B-2 40 percent.

- 1/ Includes guaranteed debt. Excludes adjusted service bonds and securities held by trust funds and agencies. Under columns A-1 and B-1 the amount in fiscal 1942 would be 11.5, under column A-2 and B-2, 16 billions. Tax revenues are assumed as in Mr. Edgerton's memorandum of March 24, 1941, except that under A-2 and B-2 still other additional taxes are assumed in fiscal 1943, to yield \$4 billions immediately.
- 2/ Holdings are the Board's figures for "Total deposits and currency in the United States", with an additional deduction of float to allow for checks in transit between payers and receivers. (The usual adjustment for float is for items in transit between banks.) The hypothetical figures in the last four columns assume, in addition to the increase in commercial banks holdings of Government securities shown in the line above, an increase in other loans and investments of 40 at commercial and savings banks and an increase in currency and/or bank reserves of 3.1; also an increase in float between depositors of 1.6.
- 3/ The hypothetical decreases are mainly for life insurance companies.
- 4/ The hypothetical changes assume in all cases that 2.0 of Government securities are purchased. Cash and marketable securities is assumed to increase 10 percent under A-1 and A-2, 20 percent under B-1 and 40 percent under B-2.
- 5/ It is assumed that money held for consumption purposes is equal to one-half month's "national income payments". See Note below table.
- 6/ This is a residual item.
- 1/ The 1936-1938 figure excludes 0.7 of adjusted service bonds. The hypothetical figures for securities to be absorbed by individuals are computed by subtracting line 2 from line 1 and further subtracting \$5 billion for securities sold to life insurance companies (2), mutual savings banks and other financial institutions (1), and nonfinancial corporations (2). The amount absorbed by individuals in the fiscal year 1942 would be about half the figure in each of the last four columns. See footnote 1 for the taxes that have been assumed.

ConfidentialB-1259  
August 11, 1941  
(Revised)ANALYSIS OF RESERVE POSITION OF MEMBER BANKS,  
WEEK ENDED WEDNESDAY, JUNE 25, 1941

by

John E. Horbett,  
Assistant Chief, Division of Bank Operations

Member bank excess reserves during the week ended June 25, 1941 amounted to approximately 5.2 billions. If reserve requirements were increased to twice basic statutory requirements (the maximum allowable under present law) excess reserves would be reduced by approximately 1.2 billions. If the law were amended and requirements were increased to two and one-half times the present basic statutory requirements, excess reserves would be reduced by 3.4 billions and would then amount to 1.8 billions. The summary figures by classes of banks are shown in the following table:

Class of banks	Excess reserves on present basis	Reduction which would result if requirements were increased to--	
		Twice basic requirements	2-1/2 times basic requirements
(Billions of dollars)			
All member banks--total	5,231	1,172	3,123
Central reserve city banks			
New York	2,202	531	1,688
Chicago	410	105	311
Large city banks	1,750	352	1,031
Country banks in places with a population of--			
200,000 or more	230	47	127
10,000-200,000	326	72	193
Under 10,000	313	65	173

An analysis has been made of the reserve position of individual member banks during the week ended June 25, 1941, and the results are shown in the accompanying statements. The analysis is based on information supplied by the Federal Reserve Banks in response to the Board's telegram of July 11. One part of the statements shows the effect of an increase in reserve requirements to twice basic statutory requirements; the other shows the effect of an increase to two and one-half times basic statutory requirements.

- 2 -

1. If reserve requirements were increased to twice basic statutory requirements-- 20%, 20%, and 14% on demand deposits and 6% on time deposits--

All but 43 member banks could meet such an increase in requirements either out of their present excess reserves or by converting up to one-half of their balances with other banks into reserve balances.

The 43 banks would have an aggregate deficiency of \$782,000 after converting one-half of their bank balances into reserve balances; 23 of them would each have a deficiency of \$5,000 or less.

The largest of these 43 banks had total assets of 27 millions, the second largest 14 millions, and the third largest 6 millions.

35 of the 43 banks were country banks located in places with a population of less than 15,000. The average ratio of loans and investments to total assets of these 35 banks was 84%, compared with 64% for all country banks and 62% for all member banks. Over one-half of these 35 banks were in the three eastern Federal Reserve districts.

A statement listing these 43 banks and showing their loans, investments, deposits, etc., on June 30 is attached. It will be observed that in nearly all cases the ratio of bank balances to deposits of these banks was considerably below that of the average bank.

1,441 banks with reserve balances less than twice basic statutory requirements could meet such an increase by converting up to one-half of their balances with other banks into reserve balances; their aggregate deficiencies before such conversion would be 67 millions.

About three-fourths of the banks whose reserve balances were not sufficient to meet an increase to twice basic requirements would have sufficient reserves after converting not more than 10 per cent of their bank balances into reserve balances. There were a few banks, however, that would not have enough reserves even after converting all of their bank balances into reserve balances. The accompanying table distributes the member banks according to the percentage of bank balances that would have to be converted into reserve balances.

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DISTRIBUTION OF MEMBER BANKS ACCORDING TO THE PERCENTAGE OF BANK BALANCES THAT WOULD HAVE TO BE CONVERTED INTO RESERVE BALANCES TO MEET AN INCREASE IN RESERVE REQUIREMENTS TO TWICE BASIC REQUIREMENTS

Class of banks	Total number of banks	Number with sufficient reserves	Number of banks that would have to convert the following percentages of bank balances into reserve balances--						
			10% or less	11-20%	21-30%	31-50%	51-70%	71-100%	Over 100%
All member banks	6,519	5,065	1,105	216	61	59	7	17	19
Central reserve city banks:			1,494						
New York	36	26	10	2	3	1	3	--	--
Chicago	12	8	4	--	2	1	1	--	--
Reserve city banks	345	265	40	60	14	4	1	--	1
Country banks in places with a population of--									
100,000 or more	199	138	6	45	9	3	3	--	--
15,000-100,000	1,001	733	24	219	32	5	7	1	2
Under 15,000	4,956	3,895	779	156	47	44	6	14	15

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2. If reserve requirements were increased to two and one-half times basic statutory requirements -- 32-1/2%, 25%, and 17-1/2% on demand deposits and 7-1/2% on time deposits--

261 member banks would have to provide additional reserves after converting one-half of their balances with other banks into reserve balances. These banks would have an aggregate deficiency of 180 millions after converting one-half of their bank balances into reserve balances.

2,977 banks with reserve balances less than two and one-half times basic statutory requirements could meet such an increase by converting up to one-half of their balances with other banks into reserve balances.

3,311 banks--about half the total number of member banks--had reserve balances sufficient to meet an increase to two and one-half times the basic statutory requirements.

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DISTRIBUTION OF HOLDINGS OF DEPOSITS AND CURRENCY 1929-1943

Hypothetical, assuming present defense policies and restriction of bank expansion

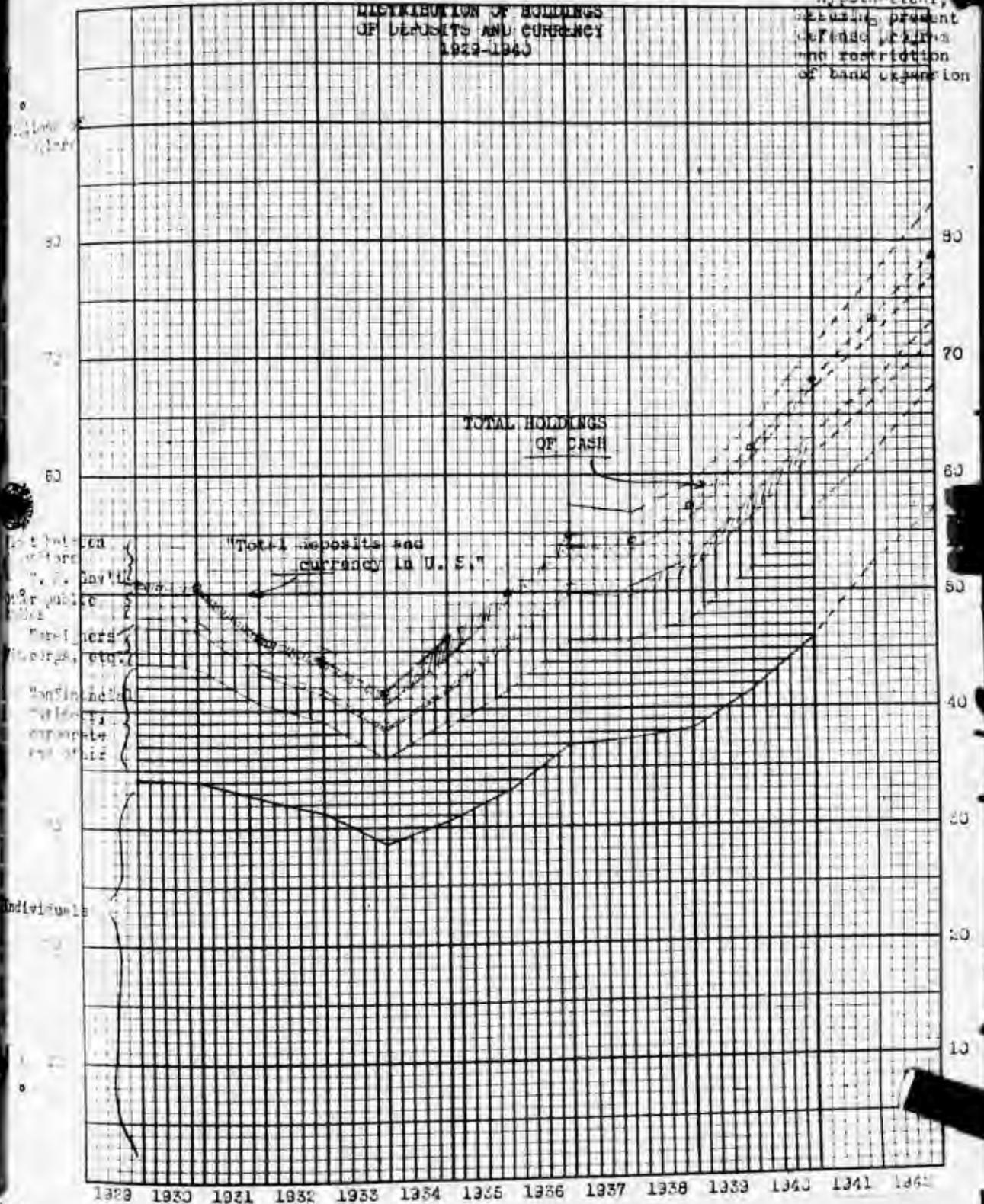
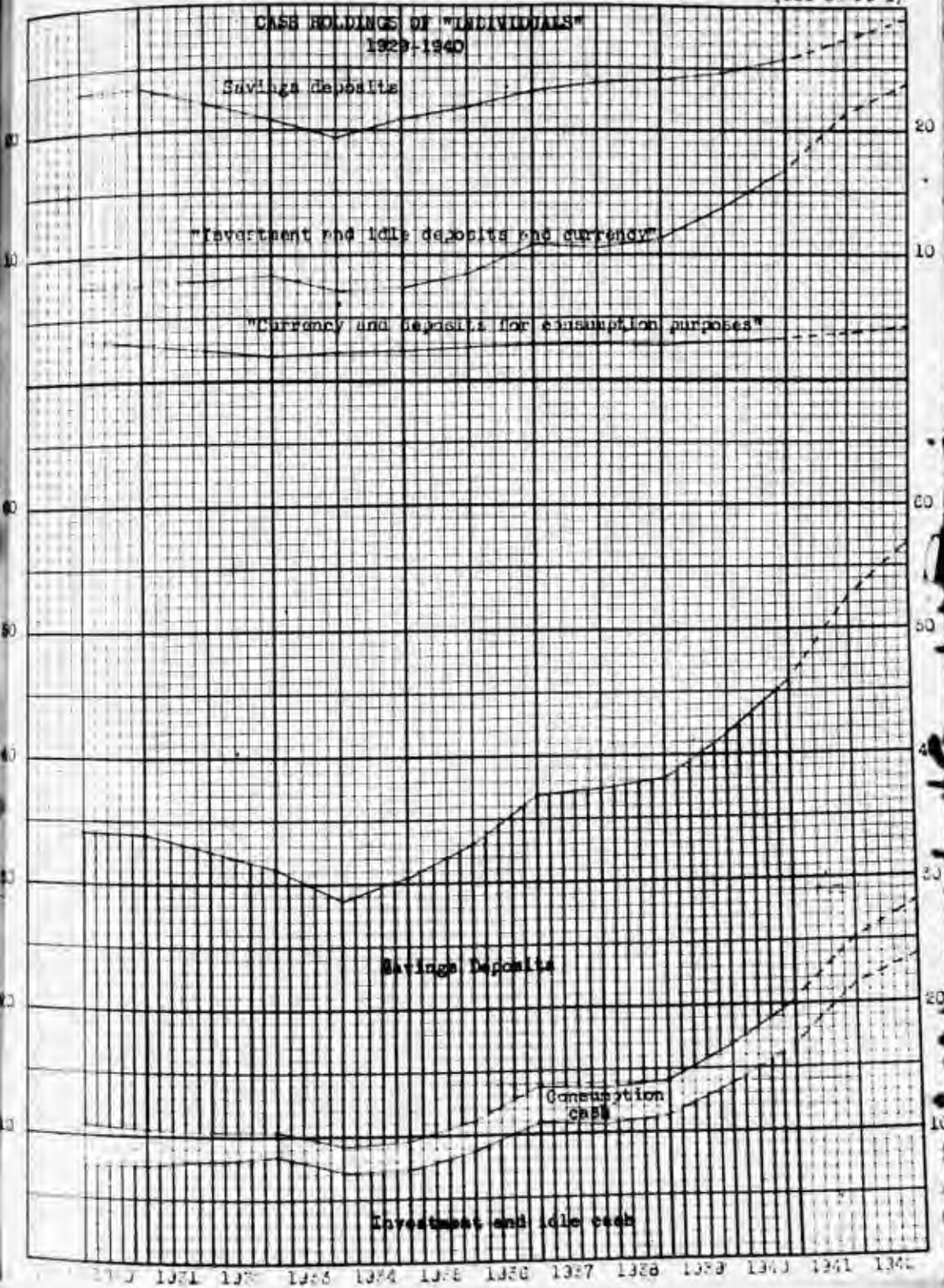


CHART 2

1945

Hypothetical  
(see chart 1)

CASH HOLDINGS OF "INDIVIDUALS"  
1929-1940



This illustrates an increase in reserve requirements to twice basic statutory reserve requirements  
(Based on averages of daily figures, amounts in thousands of dollars)

	All member banks	Central Reserve city banks		Reserve city banks	Total	Country banks		
		New York	Chicago			In pieces with a population of--		
						100,000 and over	15,000-100,000	Less than 15,000
<u>Reserve percentages, if increased to twice basic statutory requirements:</u>								
<u>On demand deposits</u>		26	26	20	14	14	14	14
<u>On time deposits</u>		6	6	6	6	6	6	6
1. Banks with reserve balances sufficient to meet the increase in reserve requirements:								
Number of banks	5,065	26	8	265	4,766	138	733	3,895
Excess reserves if requirements were increased	4,127,300	1,673,301	307,908	1,432,567	713,524	189,143	266,122	257,999
2. Banks that could meet the increase by converting not more than half of their bank balances into reserve balances:								
Number of banks	1,441	9	4	79	1,349	60	263	1,026
Deficiency in reserves before converting bank balances	-67,408	-1,974	-2,325	-34,695	-28,424	-6,566	-12,432	-9,416
Excess reserves after converting half of bank balances into reserves	540,973	2,402	2,893	213,423	322,255	80,692	151,272	90,291
3. Banks that would have to provide additional reserves after converting half of bank balances into reserve balances:								
Number of banks	43	1	--	1	41	1	5	35
Deficiency in reserves before converting bank balances	-1,230	-567	--	-52	-611	-18	-135	-468
Deficiency in reserves after converting half of bank balances into reserves	-782	-463	--	-25	-294	-14	-56	-224
4. All member banks:								
Number of banks	6,549	36	12	345	6,156	199	1,001	4,956
Excess reserves on present basis	5,230,447	2,201,546	410,160	1,749,663	869,078	229,634	326,163	313,281
Excess reserves if requirements were increased to twice basic statutory requirements	4,058,662	1,670,760	305,583	1,377,820	680,499	182,559	253,855	212,085

Note: Due to the fact that balances due from banks are deductible from demand deposits subject to reserve, a withdrawal of such balances results in some increase in required reserves. If allowance is made for this, two banks would move from group 2 to group 3 and would have small deficiencies in reserves after converting one-half of bank balances into reserve balances.

Table 1a--assuming an increase in reserve requirements to twice basic statutory requirements.

Distribution of number of banks, by classes, assuming an increase in reserve requirements to twice basic statutory requirements*	Total number	Number of banks, by Federal Reserve districts--											
		Boston	New York	Phila- delphia	Cleve- land	Rich- mond	Atlanta	Chicago	St. Louis	Stam- polis	Kansas City	De- troit	San Francisco
1. All member banks--total	6,549	316	787	655	667	437	317	880	425	452	731	570	276
a. Reserve balances sufficient	5,065	219	655	501	558	344	245	735	337	334	521	410	176
b. Reserve balances plus 1/2 bank balances sufficient	1,441	94	118	145	106	91	72	144	88	114	214	155	100
c. Reserve balances plus 1/2 bank balances insufficient	43	3	14	9	3	2	--	1	--	4	2	5	--
2. Central reserve city banks--total	48	--	36	--	--	--	--	12	--	--	--	--	--
a. Reserve balances sufficient	34	--	26	--	--	--	--	8	--	--	--	--	--
b. Reserve balances plus 1/2 bank balances sufficient	13	--	9	--	--	--	--	4	--	--	--	--	--
c. Reserve balances plus 1/2 bank balances insufficient	1	--	1	--	--	--	--	--	--	--	--	--	--
3. Reserve city banks--total	345	10	11	22	33	34	21	65	24	9	50	36	30
a. Reserve balances sufficient	265	9	8	19	30	31	12	45	17	6	36	29	23
b. Reserve balances plus 1/2 bank balances sufficient	79	1	3	3	3	2	9	20	7	3	14	7	7
c. Reserve balances plus 1/2 bank balances insufficient	1	--	--	--	--	1	--	--	--	--	--	--	--
4. Country banks, population 100,000 and over--total	199	36	40	19	26	3	11	14	17	16	6	2	9
a. Reserve balances sufficient	138	24	26	17	20	2	10	9	12	9	3	1	5
b. Reserve balances plus 1/2 bank balances sufficient	60	12	14	2	6	1	1	5	5	6	3	1	4
c. Reserve balances plus 1/2 bank balances insufficient	1	--	--	--	--	--	--	--	--	1	--	--	--
5. Country banks, population 15,000-100,000--total	1,001	106	163	92	113	73	72	151	44	50	51	46	40
a. Reserve balances sufficient	733	72	130	69	95	50	54	112	34	31	27	34	25
b. Reserve balances plus 1/2 bank balances sufficient	263	34	30	21	18	23	18	39	10	19	24	12	15
c. Reserve balances plus 1/2 bank balances insufficient	5	--	3	2	--	--	--	--	--	--	--	--	--
6. Country banks, population less than 15,000--total	4,956	194	537	522	485	327	213	638	340	377	630	466	197
a. Reserve balances sufficient	3,895	144	465	396	413	261	169	561	274	288	465	346	123
b. Reserve balances plus 1/2 bank balances sufficient	1,066	47	62	119	79	65	44	76	66	86	173	135	74
c. Reserve balances plus 1/2 bank balances insufficient	35	3	10	7	3	1	--	1	--	3	2	5	--

\*The groupings a, b, and c, under each main classification, show--

- (a) the number of banks that had reserve balances sufficient to meet an increase to twice basic statutory requirements,  
 (b) the number that could have met such an increase by converting half of their bank balances into reserve balances,  
 (c) the number that could not have met such an increase by converting half of their bank balances into reserve balances.

## ANALYSIS OF RESERVE POSITION OF MEMBER BANKS, WEEK ENDED WEDNESDAY, JUNE 25, 1941

Table 2--Assuming an increase in reserve requirements to two and one-half times basic statutory reserve requirements

(Based on averages of daily figures; amounts in thousands of dollars)

	All member banks	Central Reserve city banks		Reserve city banks	Country banks			
		New York	Chicago		Total	In places with a population of-- 100,000 and over	15,000-100,000	Less than 15,000
<u>Reserve percentages, if increased to two and one-half times basic statutory requirements:</u>								
On demand deposits		32-1/2	32-1/2	25	17-1/2	17-1/2	17-1/2	17-1/2
On time deposits		7-1/2	7-1/2	7-1/2	7-1/2	7-1/2	7-1/2	7-1/2
1. Banks with reserve balances sufficient to meet the increase in reserve requirements:								
Number of banks	3,311	16	7	147	3,141	90	409	2,562
Excess reserves if requirements were increased	2,391,655	738,454	114,538	1,002,968	535,695	142,896	199,217	193,582
2. Banks that could meet the increase by converting not more than half of their bank balances into reserve balances:								
Number of banks	2,977	6	3	180	2,788	99	481	2,208
Deficiency in reserves before converting bank balances	-340,992	-5,437	-9,463	-179,867	-146,225	-38,289	-61,200	-46,736
Excess reserves after converting half of bank balances into reserves	928,826	1/551	16,150	398,075	515,152	124,372	227,406	153,372
3. Banks that would have to provide additional reserves after converting half of bank balances into reserve balances:								
Number of banks	261	14	2	18	227	10	31	106
Deficiency in reserves before converting bank balances	-242,785	-119,601	-6,181	-104,366	-12,427	-1,998	-4,667	-6,362
Deficiency in reserves after converting half of bank balances into reserves	-180,202	-109,695	-3,767	-61,224	-5,526	-615	-2,016	-2,365
4. All member banks:								
Number of banks	6,540	36	12	345	6,156	199	1,001	4,956
Excess reserves on present basis	5,230,447	2,201,546	410,160	1,749,663	865,078	229,634	320,103	313,233
Excess reserves if requirements were increased to two and one-half times basic statutory requirements	1,807,878	613,216	98,894	718,715	377,053	103,008	133,560	110,646

Notes: Due to the fact that balances due from banks are deductible from demand deposits subject to reserve, a withdrawal of such balances results in some increase in reserve requirements. If allowance is made for this, a number of the banks in group 2 would move into group 3 and would have some deficiency in reserves after converting one-half of bank balances into reserve balances.

1/ This aggregate net deficiency is due to the increase in reserve requirements which results from a withdrawal of balances due from 5-1259 banks. (See page 276)

Table 2a--Assuming an increase in reserve requirements to two and one-half times basic statutory requirements

Distribution of number of banks, by class, assuming an increase in reserve requirements to two and one-half times basic statutory requirements*	Total number	Number of banks, by Federal Reserve district--											
		Boston	New York	Philadelphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minneapolis	Kansas City	Dallas	San Francisco
<b>1. All member banks--total</b>	<b>6,549</b>	<b>316</b>	<b>787</b>	<b>655</b>	<b>667</b>	<b>437</b>	<b>317</b>	<b>880</b>	<b>425</b>	<b>452</b>	<b>737</b>	<b>570</b>	<b>276</b>
a. Reserve balances sufficient	3,311	158	468	325	381	235	111	530	211	194	304	280	84
b. Reserve balances plus 1/2 bank balances sufficient	2,977	162	256	275	265	195	173	338	208	240	418	268	179
c. Reserve balances plus 1/2 bank balances <u>insufficient</u>	261	26	63	55	21	7	3	12	6	18	15	22	13
<b>2. Central reserve city banks--total</b>	<b>48</b>	<b>--</b>	<b>36</b>	<b>--</b>	<b>--</b>	<b>--</b>	<b>--</b>	<b>12</b>	<b>--</b>	<b>--</b>	<b>--</b>	<b>--</b>	<b>--</b>
a. Reserve balances sufficient	23	--	16	--	--	--	--	7	--	--	--	--	--
b. Reserve balances plus 1/2 bank balances sufficient	9	--	6	--	--	--	--	3	--	--	--	--	--
c. Reserve balances plus 1/2 bank balances <u>insufficient</u>	16	--	14	--	--	--	--	2	--	--	--	--	--
<b>3. Reserve city banks--total</b>	<b>315</b>	<b>10</b>	<b>11</b>	<b>22</b>	<b>33</b>	<b>31</b>	<b>21</b>	<b>65</b>	<b>24</b>	<b>9</b>	<b>50</b>	<b>36</b>	<b>30</b>
a. Reserve balances sufficient	147	8	3	12	21	19	5	28	5	2	15	17	12
b. Reserve balances plus 1/2 bank balances sufficient	180	1	5	8	12	14	15	34	16	7	34	19	15
c. Reserve balances plus 1/2 bank balances <u>insufficient</u>	18	1	3	2	--	1	1	3	3	--	1	--	3
<b>4. Country banks, population 100,000 and over--total</b>	<b>199</b>	<b>36</b>	<b>40</b>	<b>19</b>	<b>26</b>	<b>3</b>	<b>11</b>	<b>14</b>	<b>17</b>	<b>16</b>	<b>6</b>	<b>2</b>	<b>9</b>
a. Reserve balances sufficient	90	14	18	10	16	2	7	5	9	4	2	1	2
b. Reserve balances plus 1/2 bank balances sufficient	99	18	21	9	9	1	4	9	8	8	4	1	7
c. Reserve balances plus 1/2 bank balances <u>insufficient</u>	10	4	1	--	1	--	--	--	--	4	--	--	--
<b>5. Country banks, population 15,000-100,000--total</b>	<b>1,001</b>	<b>106</b>	<b>163</b>	<b>92</b>	<b>113</b>	<b>73</b>	<b>72</b>	<b>151</b>	<b>44</b>	<b>50</b>	<b>51</b>	<b>40</b>	<b>40</b>
a. Reserve balances sufficient	489	46	103	48	66	31	29	75	21	18	20	15	13
b. Reserve balances plus 1/2 bank balances sufficient	481	55	47	39	44	40	43	76	23	31	31	20	20
c. Reserve balances plus 1/2 bank balances <u>insufficient</u>	31	5	13	5	3	2	--	--	--	1	--	1	1
<b>6. Country banks, population less than 15,000--total</b>	<b>4,956</b>	<b>194</b>	<b>537</b>	<b>522</b>	<b>495</b>	<b>327</b>	<b>213</b>	<b>638</b>	<b>310</b>	<b>377</b>	<b>630</b>	<b>446</b>	<b>197</b>
a. Reserve balances sufficient	2,562	90	328	255	278	183	100	425	176	170	267	203	57
b. Reserve balances plus 1/2 bank balances sufficient	2,208	88	177	219	200	140	111	216	161	194	310	222	131
c. Reserve balances plus 1/2 bank balances <u>insufficient</u>	186	16	32	48	17	4	2	7	3	13	14	21	9

\*The groupings a, b, and c, under each main classification, show--

- the number of banks that had reserve balances sufficient to meet an increase to two and one-half times basic statutory requirements,
- the number that could have not such an increase by converting half of their bank balances into reserve balances, and
- the number that could not have not such an increase by converting half of their bank balances into reserve balances.

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ASSETS AND LIABILITIES OF MEMBER BANKS WHICH, AFTER CONVERTING HALF OF THEIR DAILY BALANCES INTO RESERVE BALANCES, WOULD HAVE TO PROVIDE ADDITIONAL RESERVES IN ORDER TO MEET AN INCREASE IN RESERVE REQUIREMENTS TO THE BASIC STATUTORY REQUIREMENTS  
(The figures of assets and liabilities are as of June 30, 1941, but the reserve analysis was based on averages of daily figures for the week ended June 25, 1941)

F. R. Dist. No.	City and State	Name of bank	Additional reserves needed	Total assets	Loans	U.S. Govt securities	Other securities	Balances due from banks	Deposits	Ratios (per cent)				
										Loans and investments to assets	Loans to assets	U.S. Govt securities to assets	Other securities to assets	Bank balances to deposits
<b>CENTRAL RESERVE CITY BANK</b>														
2	New York, N.Y.	Solroder Trust Company	463	27,128	4,145	12,093	3,619	270	23,375	73.2	15.3	14.6	13.3	1.2
<b>RESERVE CITY BANK</b>														
5	Baltimore, Md.	Calvert Bank	25	13,908	2,723	3,836	2,776	148	12,630	67.1	19.6	27.6	20.0	1.2
<b>COUNTRY BANK IN A PLACE WITH A POPULATION OF 100,000 OR MORE</b>														
9	Minneapolis, Minn.	Fidelity State Bank	14	2,636	1,870	205	299	9	2,467	88.5	70.9	7.8	13.6	.4
<b>COUNTRY BANKS IN PLACES WITH A POPULATION OF 15,000-100,000</b>														
2	Groenwich, Conn.	First National Bank	13	4,886	2,212	1,742	53	77	4,168	82.0	45.3	35.7	1.1	1.7
2	Hackensack, N.J.	Bergen County National Bank	6	3,541	1,504	723	667	35	3,095	81.7	42.5	20.4	16.6	1.1
2	Middletown, N.Y.	National Bank of	15	4,607	1,312	1,927	170	110	4,034	81.2	29.1	41.8	10.2	2.7
2	Shamokin, Pa.	West End National Bank	5	1,659	423	263	628	55	1,369	79.2	25.4	15.8	37.8	4.0
3	Shamokin, Pa.	National-Dime Bank	17	4,838	1,563	1,038	975	19	3,864	73.9	32.3	21.5	20.2	1.3
Total, 5 country banks in places with a population of 15,000-100,000			56	19,531	7,044	5,693	2,793	326	16,850	79.5	36.1	29.1	14.3	1.9
<b>COUNTRY BANKS IN PLACES WITH A POPULATION OF LESS THAN 15,000</b>														
1	Lebanon, N. H.	National Bank of	10	1,080	462	231	80	30	854	71.6	42.8	21.4	7.4	3.5
1	Enosburg Falls, Vt.	Enosburg Falls National Bank	5	454	305	8	76	10	369	85.7	67.2	1.8	16.7	2.7
1	Poultney, Vt.	Poultney National Bank	11	769	573	27	35	16	649	82.6	74.5	3.5	4.6	2.5
2	Cato, N. Y.	First National Bank	5	606	402	74	69	6	511	89.9	66.3	12.2	11.4	1.2
2	Dolhi, N. Y.	Delaware National Bank	17	1,883	1,067	388	106	9	1,650	88.9	96.7	20.6	5.6	.5
2	Florida, N. Y.	National Bank of Florida	5	714	452	92	35	25	605	79.7	63.3	12.9	4.9	1.1
2	Hendon, N. Y.	First National Bank	7	630	435	26	50	3	481	81.1	69.0	4.1	7.9	.6
2	Harrisville, N.Y.	First National Bank	4	362	174	54	78	2	292	84.5	46.1	14.9	21.5	.7

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(The figures of assets and liabilities are as of June 30, 1941, but the reserve analysis was based on averages of daily figures for the week ended June 25, 1941)

F. R. Dist. No.	City and State	Name of bank	Additional reserves needed <sup>1/</sup>	Total assets	Loans	U.S. Govt. securities	Other securities	Balances due from banks	Deposits	Ratios (per cent)					
										Loans and investments to assets	Loans to assets	U.S. Govt. securities to assets	Other securities to assets	Bank balances to deposits	
											In thousands of dollars				
(Continued)															
2	Herman, N. Y.	First National Bank	2	124	222	51	59	2	319	78.3	52.4	12.0	13.9	.6	
2	Ricksville, N.Y.	Long Island National Bank	8	1,444	1,143	4	53	31	1,151	83.1	79.2	.3	3.7	2.7	
2	Liberty, N. Y.	National Bank of	21	2,878	1,372	516	631	37	2,495	87.5	47.7	17.9	21.9	1.5	
2	Ransom, N. Y.	First National Bank	3	701	118	292	203	11	620	87.4	19.2	11.7	29.0	1.8	
2	Warronsburg, N.Y.	Warren National Bank	8	1,366	893	75	144	11	1,197	81.4	65.4	5.5	10.5	.9	
3	Tom's River, N. J.	First National Bank	13	5,604	3,136	672	984	53	4,537	85.5	56.0	12.0	17.5	1.2	
3	Bakerton, Pa.	First National Bank	4	529	154	218	68	13	436	83.2	29.1	41.2	12.9	3.0	
3	Catawissa, Pa.	Catawissa National Bank	14	912	715	28	45	2	690	86.4	78.4	3.1	4.9	.3	
3	Dauphin, Pa.	Dauphin National Bank	1	270	168	25	28	4	223	81.9	62.2	9.3	10.3	1.8	
3	Martinsburg, Pa.	First National Bank	1	264	130	25	42	4	225	74.6	49.2	9.5	15.9	1.8	
3	Ulster, Pa.	First National Bank	2	506	169	39	219	15	419	84.4	33.4	7.7	43.3	3.6	
3	Weatherly, Pa.	First National Bank	2	706	329	64	140	12	583	73.5	46.6	9.1	19.8	2.1	
4	Georgetown, Ky.	First National Bank	4	643	255	118	43	52	545	69.5	39.7	23.2	6.7	9.5	
4	Waco, Pa.	Second National Bank	2	1,035	277	268	317	32	913	83.3	26.8	25.9	30.6	3.5	
4	Stoytown, Pa.	First National Bank	1	299	174	17	57	2	218	82.9	58.2	5.7	19.1	.9	
5	Lorington, Va.	Rockbridge National Bank	4	1,978	1,240	293	105	75	1,702	82.8	62.7	14.8	5.3	4.4	
7	Battle Ground, Ind.	Battle Ground State Bank	3	347	243	40	2	25	291	82.1	70.0	11.5	.6	8.6	
9	London, S. D.	First National Bank	6	681	319	236	19	18	607	84.3	46.8	34.7	2.8	3.0	
9	Manistique, Mich.	State Savings Bank	8	808	424	121	122	20	723	82.5	52.5	15.0	15.1	2.8	
9	Stephen, Minn.	First National Bank	1	372	237	55	36	5	327	88.1	63.7	14.8	9.7	1.5	
10	St. Marys, Kans.	St. Marys State Bank	2	598	377	107	25	30	498	85.1	63.0	17.9	4.2	6.0	
10	Granite, Okla.	First National Bank	1	283	138	20	84	5	237	85.5	48.8	7.1	29.7	2.1	
11	Ammon, Tex.	First National Bank	3	109	24	-0-	3	6	70	79.8	77.1	--	2.8	8.6	
11	Cameron, Tex.	Citizens National Bank	30	6,030	598	908	3,914	121	5,787	89.9	9.9	15.1	64.9	2.1	
11	Dodson, Tex.	First State Bank	1	192	136	25	1	6	120	84.3	70.8	13.0	.5	5.0	

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(R.vised)

Regraded Unclassified

ASSETS AND LIABILITIES OF MEMBER BANKS WHICH, AFTER CONVERTING HALF OF THEIR BANK BALANCES INTO RESERVE BALANCES, WOULD HAVE TO MAINTAIN ADDITIONAL RESERVES IN ORDER TO MEET AN INCREASE IN RESERVE REQUIREMENTS TO TWICE BASIC STATUTORY REQUIREMENTS

(The figures of assets and liabilities are as of June 30, 1941, but the reserve analysis was based on average of daily figures for the week ended June 25, 1941)

F. R. Dist. No.	City and State	Name of bank	Additional reserves needed <sup>1/</sup>	Total assets	Loans	U. S. Govt. securities	Other securities	Balances due from banks	Deposits	Ratios (per cent)				
										Loans and investments to assets	Loans to assets	U.S. Govt. securities to assets	Other securities to assets	Bank balances to deposits
In thousands of dollars														
(Continued)														
11	Dumas, Tex.	First State Bank	13	543	364	38	26	56	489	78.6	67.0	7.0	4.6	11.5
11	Oglosby, Tex.	First National Bank	2	143	87	7	7	24	108	70.6	60.8	4.9	4.9	22.2
Total, 35 country banks in places with a population of less than 15,000			224	36,163	17,372	5,193	7,906	773	30,941	64.3	48.0	14.4	21.9	2.5
Total, 41 country banks			294	58,330	26,286	11,091	10,958	1,108	50,258	62.9	45.1	19.0	17.7	2.2
Average ratios for all country banks, Apr. 4, 1941			.....	.....	.....	.....	.....	.....	.....	64.3	31.3	20.0	13.0	19.5
Grand Total, 43 banks			782	99,366	33,152	27,020	17,353	1,526	86,263	78.0	33.4	27.2	17.4	1.8

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<sup>1/</sup> After converting one-half of bank balances into reserve balances.

\* Average balances due from banks, as reported for the week ended June 25, 1941, were considerably below the amount shown in the June 30 call report.

September 3, 1941  
2:30 p.m.

HMJr: Hello.

Operator: Mrs. Klotz is back now.

HMJr: Where's Mr. Henderson?

Operator: I have him right here. Go ahead.

HMJr: Hello.

Leon Henderson: Hello. Did you have a good rest?

HMJr: Yes, I did. Is this Leon?

H: Yes.

HMJr: How are you?

H: I'm in pretty good shape.

HMJr: Say, Leon, this is something that normally I'd rather talk to you about across the table, but I'm sure it was an oversight on your part. Remember you and I had sort of a gentlemen's agreement as to that business of Ways and Means, that if you were going to do anything on taxes, you'd talk to me first?

H: Yeah.

HMJr: Well, Senator George has sent me down this correspondence from you on joint returns.....

H: Yeah.

HMJr: .....and calling a spade a spade - I mean, I just think it - that wasn't the understanding you and I had.

H: Oh, why then - then that's my fault, Henry. I meant about testifying.

HMJr: Oh.

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H: All we did was this. We did some work on joint returns.....

HMJr: Yeah.

H: .....and I had spoken about it and the fellows worked it up and came in here one morning.....

HMJr: Yeah.

H: .....and asked me whether it wouldn't be a good thing to send it on down to him.....

HMJr: Yeah.

H: .....and I didn't think - I was busy, and didn't think anything more about it.

HMJr: Yeah.

H: That's the only thing we've sent down. I thought - I meant about.....

HMJr: Well.....

H: I had in mind testifying. It never occurred to me on this thing.

HMJr: Well, frankly George didn't seem to sort of like it and.....

H: What?

HMJr: .....he didn't kind of like it, see? And I thought I'd - normally I'd sit down, but I didn't want to take up your time.

H: Well, you can rest assured on that. That's the only thing we've done.....

HMJr: Yeah.

H: .....and I won't do any more of them - even what seems as harmless as that. It looked to me as just a little technical work.

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HMJr: Well, you know how hard it is keeping your own stable.

H: Sure. It was.....

HMJr: I'm not making a.....

H: It was absolutely an oversight on my part.

HMJr: I'm sure it was.

H: And.....

HMJr: Now, in return, Leon, that price statement which they wouldn't let me give before the Committee.....

H: Yeah.

HMJr: I'm going to give it Tuesday night in Boston.

H: You're going to be called as a witness one of these days.

HMJr: I know. But I'm going to say all the things up there that they wouldn't let me say. And sometime - hello.

H: They didn't get to you.

HMJr: I know, but.....

H: They haven't finished with me yet, you know.

HMJr: No. But sometime I'll tell you why I think they called me off.

H: Well, I don't think there - there wasn't any - there wasn't anything back of that. It was just they had not - they wouldn't let go of me.

HMJr: They wouldn't?

H: No. There was - there's no hidden reason that I can see.

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HMJr: Well, I personally - I don't know. Maybe it's just suspicion, but I think - I showed the thing to three fellows from the Department of Agriculture.....

H: Uh huh.

HMJr: .....and within the same day Ed O'Neal got very interested in what I was doing.

H: Uh huh.

HMJr: Hello.

H: Yeah. Well, I don't - this had nothing - it may have.

HMJr: Then the next thing I knew was they didn't want me.

H: Well.....

HMJr: But anyway, I'm going to give this; and I'd like very much if Ferdie Kuhn could come over and show it to you tomorrow.....

H: All right

HMJr: .....and get.....

H: Well, it better be in the morning, because in the afternoon I'll be before the Maloney Committee on this oil business.

HMJr: Well, then he - it won't be ready, so maybe - would you want to take it home or would you want it Friday morning?

H: Well, when - I'll tell you. When Ferdie gets it done - when you get it done, why don't he call me and we'll decide then.

HMJr: All right. I'll send one copy to you and one to Miss Elliott.

H: All right.

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HMJr: Because she was very helpful when you were up on the Hill.

H: All right.

HMJr: But I'm sure there's nothing in there but what you'd like, but there might be, and you might have some good suggestions.

H: All right. Well, then, consider that I've apologized for violating.....

HMJr: Well.....

H: .....as I say, the boys had been working on it.....

HMJr: Yeah.

H: .....and I didn't - they brought it in one morning and said, "How about sending this to George?" I sat thinking about it and I signed a note and out it went and out of mind even.

HMJr: I - well, so much for that. I mean, there's so much to do you and I can't afford to have any squabbles.

H: That's right. That's right.

HMJr: Let me ask you this. Are you happy over the new setup?

H: I'm happy in that it's - we - you've got a spirit of working.....

HMJr: Yeah.

H: .....and Don has taken hold, and I'm happy about that.....

HMJr: Yeah.

H: I'm not - I would rather have had a full-time working Board.....

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HMJr: Yeah.

H: .....that is, it's a full-time job, as I see it.....

HMJr: Yeah.

H: .....not something for busy people to do.

HMJr: No.

H: I'm not so happy with the prospect of three jobs that I've got when price is about enough.....

HMJr: Yeah.

H: .....but we were short on material, Henry, for these civilian supply jobs.....

HMJr: I see.

H: And it's going to mean an extra load for me, but it's got more promise in it than anything we've ever seen.

HMJr: Good. Good.

H: Say, if you've got your pencil there - if your girl's on I've got a new number.

HMJr: No, the girl's not on.

H: Well, that's all right. Republic 0154.

HMJr: Wait a minute. Republic.....

H: 0154.

HMJr: Say it again.

H: Republic.....

HMJr: Yeah.

H: 01.....

HMJr: 01.

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H: 54.  
HMJr: 0154 - Republic.  
H: Yeah. That's my desk's private number.  
HMJr: 0154 - I'll give it to her.  
H: All right, Henry.  
HMJr: Take care of yourself.  
H: All right, fella.  
HMJr: Good-bye.  
H: Good-bye.

MEMORANDUM

September 3, 1941.

TO: Secretary Morgenthau  
FROM: Mr. Sullivan

J.S.

At noon today the Senate Finance Committee took up the tax bill and before recessing at three o'clock this afternoon they had tentatively agreed on everything in the bill except the following items, which were passed over because they were controversial and will be taken up when the Senate meets tomorrow forenoon at eleven o'clock:

- Lowered personal exemptions,
- Repeal of the special 10% excess profits tax,
- Community property,
- Estate and gift taxes,
- Admissions tax,
- Coin operated devices,
- Social Security tax amendments.

There is a possibility that the wine tax may be reopened, although it was tentatively agreed to this afternoon.

I talked with Senator Berkley about wiring absent senators to return and he said everyone had been wired last night. He agreed, however, to wire them again this afternoon.

September 3, 1941  
3:30 p.m.

RE DEFENSE SAVINGS STAFF

Present: Mr. Sloan  
Mr. Buckley  
Mr. Kuhn  
Mr. Callahan  
Mr. McCarty  
Mr. Pulte  
Mr. Olney  
Mr. Duffus  
Mr. Mahan  
Mr. Edward  
Mr. Sparks  
Mr. Graves

Graves: Have you anything particular you would like to ask me about?

H.M.Jr: Oh, as we go along I have got a little - I have got no list.

Graves: To start off with?

H.M.Jr: No list of complaints.

Graves: I think we might begin, then --

H.M.Jr: I have got one little one. I never heard from Cole Porter. Did you write him a letter?

Kuhn: After you left, Mr. Secretary, Jerome Kern wrote saying that he was doing a song and he was going to get together with Gershwin, but I never saw a letter from Porter.

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Callahan: I think we asked Mr. Gershwin first and he said that he could work much better with Jerome Kern and we couldn't very well tell him that we insisted on Cole Porter. I don't know whether there is anything between them or not.

H.M.Jr: Who is going to do the song now?

Callahan: Gershwin and Kern.

H.M.Jr: That is all right.

Kuhn: Couldn't get anyone better.

H.M.Jr: How about a follow up on it?

Callahan: What do you mean?

H.M.Jr: Write Gershwin how he is coming.

Callahan: Both of them wrote in the other day and said they were getting together on it and they hoped to give us a report in a week or ten days.

H.M.Jr: Wonderful. That is all I have got. I will think of some things as we go along.

Graves: Yes, sir. Then Mr. Mahan might tell us about postage. You asked me the other day about the status of that and I told you and I will let Mr. Mahan confirm that.

Mahan: Mr. Secretary, we have been concentrating on the distribution --

H.M.Jr: Where is Sloan?

Graves: Sloan stayed outside for a minute to take care of some other business.

H.M.Jr: All right.

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Mahan: We have been concentrating on the retail posters. It has been probably the greatest distribution of display material that has ever been made. There have been around three million pieces distributed and arrangements made for those pieces to be picked up and actually delivered to retailers, as Mr. Pulte will tell you later. Now, as you know, there were a million and a half of the Minute Man posters distributed. There have been ten thousand of the "Buy a Share in America" posters and there is another hundred thousand on order that will be distributed in about ten days, approximately.

H.M.Jr: Do they like that poster?

Mahan: Like it very much.

H.M.Jr: I mean the "Buy a Share in America".

Mahan: We have had very good comments on it and it shows up very well. I saw one in Mr. Sparks' bank. He stole one of the first that was issued and it looked very well in the frame. It looked better than the other poster, I think.

We have ordered a hundred thousand more of those in the large size and a hundred thousand in the small size. Both of those are due in ten days. We have ordered ten thousand of the prize winning poster as a pilot quantity for distribution to the states and to get the comment on that poster, and then we are going to order a quantity of those for payroll allotment posting. That is a particularly good one with the two hands and so forth.

H.M.Jr: That is all right. It is very good.

- Graves: You mean, Mr. Mahan, to be put out in the factories and plants?
- Mahan: Yes, in connection - ask about our payroll allotment plan. That is a particularly good poster for that. I think the important thing is the three million pieces that have been distributed ready for this September fifteenth show. Now, we might cover albums too.
- H.M.Jr: We don't begin to have anything like the coverage they do in Canada, for instance. I mean, you can't go anywhere in Canada but what you are conscious all the time of their savings posters. It is the only poster they have but you bump into it every where you go, which you don't with ours.
- Mahan: That is the best distribution we will have, is this three million. That will mean practically every retail store of any size is covered, not with one but with several. On the ten cent album which we wanted to have ready at the opening of school, ten million of those are now on their way to post offices and fifteen million additional have been ordered so that as that supply is used up we will have a new one coming and and we think that is very important as a part of this retail activity, to have it - as many children as possible with albums.
- Graves: I might say this. I don't know whether you knew, but when we ordered stamp albums to begin with we did not order anything for the ten cent stamp.
- H.M.Jr: You did not?
- Graves: We did not, and we have had great demand for the same kind of album in the ten cent stamp that we have had all the time for

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the other denominations and this represents the initial supply of ten cent albums.

- Mahan: That is right, first album. There was one other activity this morning on - the Cunningham Drug Stores want to print two hundred thousand copies of the song themselves at their own expense and offer it both through full page newspaper ads and also over the radio.
- H.M.Jr: Where are those stores?
- Mahan: In Detroit and Michigan. They have stores throughout Michigan. They were very very helpful.
- H.M.Jr: Got any more whiskey ads?
- Mahan: I don't know about the whiskey situation.
- H.M.Jr: Who put that field over?
- Graves: Do you know about it, Sid, the Seagram ad?
- Mahan: No, I don't know about it. I have simply seen it. I don't know what the circumstances are. As a matter of fact, the representative is going to be down tomorrow.
- Graves: They did that on their own, I assume, without any --
- Mahan: I think so. We will know tomorrow. But I think --
- Sparks: They phoned for a meeting for tomorrow to talk over a plan that they had but at that time they said nothing about publishing an advertisement.
- H.M.Jr: It is not too good.

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- Mahan: I think we are perfectly agreeable to this, though.
- H.M.Jr: That is all right.
- Mahan: Fine. I think that is everything, Mr. Graves.
- Graves: Is there anything further about the distribution of the song that you know about, Sid?
- Mahan: No.
- Buckley: I have a record on the total number distributed, if that is what you mean.
- Graves: Yes, that is right.
- H.M.Jr: The last I heard it was a hundred and seventy-eight thousand. That is the memo you (Sloan) sent me, is that right?
- Buckley: We have sent out so far about a hundred and eighty-five thousand but there are forty-five thousand cards that haven't been counted yet. They sort of pile up on us. That gives us a total of about one hundred and seventy-five thousand cards received and a hundred and eighty-five sent out, not including the forty-five thousand that haven't been counted. If there was just one apiece it would bring it up to something around about two hundred thirty thousand.
- H.M.Jr: There is something wrong with our mailing list. He tells me that twenty thousand postal cards have been returned on account of the wrong address.
- Buckley: Eighteen thousand five hundred ninety-five, up to this point.
- Graves: Is that disproportionate?

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- Buckley: It is out of two million. One percent of two million would be twenty thousand, wouldn't it?
- Graves: Yes.
- Buckley: I don't think that is out of line.
- H.M.Jr: One percent of --
- Buckley: It is out of line of a customers' list. It wouldn't be out of line of a prospects' list. This isn't quite one percent. But it isn't - ordinarily that wouldn't be considered out of line.
- H.M.Jr: But that list is supposed to be kept up to date.
- Graves: But no closer than that. I doubt if it ever would be any more nearly correct than that one percent that this is developing.
- H.M.Jr: All right.
- Buckley: This of course gives us a chance to check our list, too, which is a good thing, and bring it up to date automatically.
- Graves: I think Mr. Pulte should tell you some details about this Retailers for Defense Week.
- H.M.Jr: Go ahead.
- Pulte: Well, the Retailers for Defense Week, Mr. Secretary, is opening on September fifteenth, continuing until the twentieth. We expect by that time to have five hundred thousand retail stores cooperating in the selling of Defense Savings Stamps. Every one of the

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forty-eight states now has material that is being distributed through various sources to the retail merchants. In connection with that, President Roosevelt has issued a proclamation for the week reading, "Retailers for Defense Week, to aid in the sale of Defense Savings Stamps."

H.M. Jr:

Did he issue that?

Pulte:

He issued that proclamation. It appeared in the Sunday morning Times, the New York Times, it appeared in papers all over the country. Where we have Defense Savings committees, that is, local committees, they have handled the contact with the merchants through the merchants associations, various trade associations, Chambers of Commerce, and other groups. They have made arrangements for the distribution of material and arrangements for the retailers to obtain Defense Savings Stamps from their post offices or having wholesalers buy the stamps and re-sell them to the retailer for sale to the consumer.

Where we are not organized, Chambers of Commerce and merchants groups have worked hand in hand with the retailers and with the newspapers in arranging for the distribution of material and also working with the postmasters very closely in the towns for distribution of the Defense Savings Stamps and we are - there is an indication of how close their cooperation is being extended. Chambers of Commerce are contacting the post offices to find out how many stamps they have got on hand before the drives open so the post offices can order sufficient stamps. As an example of distribution, also, large companies - for instance, the Standard Brands Corporation

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of New York - have you heard about that?

H.M.Jr: Mr. Sloan wrote me a very excellent memorandum and brought me up to date on all this stuff.

Pulte: Then I am just reiterating.

H.M.Jr: I read it and I guess I remember it.

Pulte: Well, then, I will sum it up by saying that --

H.M.Jr: You have really got to give me something that is pretty new because Sloan did a good job.

Pulte: Then I will give you something that is new, I hope. In Michigan the retail stores from a period of July tenth to July thirty-first averaged about a dollar per day in sales of stamps. That is, the chain stores, the records we have.

H.M.Jr: A dollar a day?

Graves: Per store?

H.M.Jr: Do you think that is good?

Pulte: We think it is because it has a cumulative effect. It starts people off buying stamps.

H.M.Jr: What period?

Pulte: July tenth to July thirty-first, a twenty day period.

H.M.Jr: It sounds terrible to me.

Pulte: Well --

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- Graves: I don't think it is. The sales of stamps - we have of course no report yet for August, but sales of stamps in May, June and July ran roughly three million dollars per month. Is that right?
- Pulte: That is right.
- Graves: Now, suppose you have five hundred thousand outlets and suppose that average should be maintained. I doubt if it will, but suppose it should be. That is a half million dollars a day or twelve or fifteen million dollars a month as against three million, which has been the rate of sale, or was the rate of sale for the first three months.
- H.M.Jr: Say that again.
- Graves: Assume that this dollar a day that Mr. Pulte says was the average in Michigan - assume that dollar a day is attained by the five hundred thousand outlets that we will have selling stamps from the fifteenth of September. That would give us a half million dollars a day, or from twelve to fifteen million dollars a month for stamps, compared with three million dollars a month which was the rate of sale of stamps during May, June and July.
- H.M.Jr: Now let me give you a few figures, see. Here is my problem. You might as well get my problem. The Bureau of the Budget says we are going to spend twenty-two billion dollars. The tax bill may raise twelve billion dollars. It leaves ten billion dollars I have got to raise and the thing that I have got to figure is how much I am going to raise through this organization

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plus Tax Anticipation certificates and how much I have got to go out and borrow from the banks, so that is the thing that I have.

Graves: Well, on the stamp thing, I view it this way, that --

H.M.Jr: We can't do it all by stamps.

Graves: No, no, it is cumulative. That lays a foundation for the purchase of bonds which will become increasingly effective as time goes on. I think people will get in the habit of buying their stamps at the stores. You are going to find that dollar a day --

H.M.Jr: Oh, I am for this. You and I hoped we would have fifty thousand stores by the first of September.

Graves: I guess we had them.

Mahan: I am sure we have them.

Pulte: Oh, we have more than that.

H.M.Jr: But when you say a dollar a day per store, it seems awfully little, that is all.

Graves: That is right. It does.

H.M.Jr: It seems awfully little.

Mahan: I think that is partly accounted for, Mr. Secretary, by the fact that a great many of them were not selling right from the outset. They probably - there was probably a lag in there of several days in the case of many stores.

H.M.Jr: I wouldn't have raised the point except it

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was said as though it was to impress me and the only way it impressed me was as to how little.

Graves: I don't think he intended to impress you, just inform you.

Pulte: That was all, inform you.

H.M.Jr: O.K. I was impressed if you have fifty thousand stores and I will be overcome if you have five hundred thousand stores by the first of October.

Graves: Merely putting stamps on sale in retail stores doesn't by any means insure the sale of stamps. We have got to get going with these local community committees everywhere before we can expect to have the maximum possible result. Does that finish you up, Mr. Pulte?

Pulte: Yes, I think it does, Mr. Graves.

Graves: Supposing Mr. Buckley tells us about the mail order thing.

H.M.Jr: Don't misunderstand me. I wouldn't have said anything about the dollar. If you have got your fifty thousand by the first of September, I am delighted. If you have two hundred fifty thousand by the first of October, I will be very much pleased, and if you get your five hundred thousand by the first of January, I would be very much pleased.

Pulte: Well, the cooperation has been so splendid that - and the pledges of cooperation from organizations of retailers all over the United States indicate that five hundred thousand or more merchants by September fifteenth

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will be selling stamps.

- H.M.Jr: Well, if it is, it is amazing, an amazing achievement.
- Graves: By the way, Mr. Sloan or Mr. Mahan, what is this invitation to the Secretary to appear at the - at a meeting of these retail people again?
- Mahan: That is September fifteenth, a clinic to be held at the Mayflower Hotel from two until five o'clock and we will have on exhibit there everything pertaining to stamps and there will be speeches made by several of the prominent retailers, in which I hope they will indicate we are going to have our five hundred thousand and quite a program has been arranged preceding the Don Nelson dinner and the committee would very much like to have you open that shindig if you would, Mr. Secretary, and say a few words of welcome to them.
- H.M.Jr: What is the Don Nelson dinner?
- Mahan: That I do not know much of in detail. It is a dinner, I believe, given by the National Retail Dry Goods Association to their honorary president. It is entirely a merchants --
- H.M.Jr: If I am here on the fifteenth I will do it.
- Mahan: That would be fine.
- Kuhn: Isn't that the day you testify on the Hill?
- H.M.Jr: Supposedly. I won't be here on the sixteenth. This would be in the afternoon?

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Mahan: Yes.

H.M.Jr: They will still be sober at two, won't they?  
(Laughter)

Mahan: We would like to, of course, have you open it, if you will. That would please the boys very much.

H.M.Jr: Well, if I am here, Harold, I will do it.

Graves: Fine.

Mahan: Fine.

Graves: Now, Mr. Buckley.

Buckley: This report, Mr. Secretary, is based on a complete picture of what has been accomplished in the Mail Order Division of the Defense Savings Staff since its inception last spring. The chart of activities includes:

"(1) Regular Purchasers - those who, as the result of previous solicitation, are buying at regular intervals. To this list (approximately 100,000 at the present time), we are starting this month to send a special letter and three order forms, asking their cooperation in bringing the bonds to the attention of others.

"(2) Customers - all those who have bought but who haven't agreed to buy regularly. To this list (approximately 2,000,000 as of July 31st), we are sending a letter urging adoption of the Regular Purchase Plan, a colorful folder and a Regular Purchase order form. These start going out this Friday, September 5th.

"(3) Prospects - large investors - taken from the Customer and I. R. files. To this list

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(375,000 corporations, partnerships, associations, etc.), we have just sent a special mailing consisting of a letter, order form and folder featuring F and G bonds.

"(4) Prospects - smaller investors. These are the I. R. names (approximately 4,874,000 as of July 31st) that we are testing - in a variety of different ways - in order to find the formula that will produce maximum results.

"Before we discuss the results of our testing to date, let me raise one point that seems to me to be vitally important. In one sense, this mail order campaign - including all of our mail selling efforts - is different from practically all others. In any commercial mail order business, the product is available only by mail and results are measured in but two ways - the mail orders that come back and the repeat business that follows.

"In this mail order campaign of ours, results should be determined by :

- "(1) The number of people who are induced to send their orders direct.
- "(2) The amount of money received in relation to the cost of getting it.
- "(3) The amount of potential repeat business that becomes available at a very low selling cost.
- "(4) Equally important - the educational work done on the entire list.

"Thus, from Test Series No. 1 for instance, which went out June 21st, it should be remembered that in addition to getting 300 people to buy over \$140,000 worth of bonds at a cost of 85/100th of 1 percent, the mailing called on 94,256 other people - told them the entire

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Savings Bond story, and provided one more link in the chain of publicity and advertising being used to raise money for national defense.

"From Series One, relative returns mean more than total orders or dollars received. We put these ten tests in the mail, with existing material, to find out things and from that standpoint, they accomplished their purpose.

"We learned, for instance, that it was safe for us to circularize on Defense Savings Staff stationery; that a mailing on E bonds was as good, if not slightly better, than a mailing on all three bonds; that there was an extremely small demand for F bonds. We also learned that if our best test had been sent to the entire list, the selling cost would have been down to 73 cents for each \$100 worth of bonds sold.

"That should represent a maximum selling cost for future mailings, since none of the assemblies in Series No. 1 contained specifically prepared mail order material, and had the further disadvantage of being sent out during one of the poorest mail selling seasons of the entire year.

"From Series Two, which went into the mails July 19th, we are likewise getting some useful information. While returns are incomplete, it seems safe to conclude that the best test, both from the standpoint of orders and dollars received, will be an E mailing - thus confirming what we discovered in Series No. 1. We have also learned that with all other factors being equal, our new folder "How to Buy a Share in America" is outpulling the blue and white Defense folder used in the first tests; that the State of Massachusetts produces twice as

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many orders as the State of Michigan; that a combination of letter, folder and order form.

"From Series No. Three, which went into the mail last Saturday, August 30th, we will get a comparison between the pulling power of I.R. names with incomes over \$5,000, incomes under \$5,000 and a mixture of the two. This list check-up is being made in California, Georgia and Maryland. Also being tested are several new letters; an advertising message on the envelope versus a plain window envelope; and as another confirmation, the pulling power of E bands versus all three.

"This third series is going out at a very favorable time. In a comparatively short while it should give us an indication of the returns that can be expected from the approximately 2,000,000 new over \$5,000 names that have just been put on plates, as compared with the greater number of under \$5,000 names that are available if it is found desirable to circularize them."

H.M.Jr: I have no comment.

Graves: Mr. Duffus?

H.M.Jr: Only where the hell is the movie on "Any Bonds Today?" for the newsreels?

Duffus: Well, it was my understanding, sir, that that was discontinued. I will contact Mr. Dietz tomorrow morning and find out about that, but I thought that was dropped because of that one of Barry Wood. I thought they were letting that go. I will follow through on that tomorrow.

H.M.Jr: He said he was going to do us a good one.

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- Duffus: I will find out about that right away.
- H.M.Jr: He said that song track was all right and forget about the photographer.
- Duffus: I will check on that in the morning and give you an answer on that tomorrow.
- H.M.Jr: That was what I heard.
- Duffus: That was my understanding from Mr. Dietz, that it was discontinued after his talk.
- H.M.Jr: Maybe that - he said, now, was the sound track all right? It was fine. He said, "Forget the photography and let me take care of that." That is the last I heard.
- Duffus: I will find out about that. We opened Treasury House in New York this noon at Rockefeller Plaza with Colonel Patterson introducing. First they had a band and then Colonel Patterson introduced Mr. Willkie, who introduced Mrs. Hull, who cut the ribbon. I talked with them two hours after it was opened. They have had a continual sale of stamps, the crowd was so big. We open a similar House tomorrow in Boston.
- H.M.Jr: Who is responsible for putting it in Rockefeller Plaza?
- Duffus: The Esso people.
- H.M.Jr: Wouldn't they go to Fourteenth Street or Twenty-third?
- Duffus: We told them it was our wish that it be at either Fourteenth Street or Twenty-third, but in a meeting in Colonel Patterson's office they said they wanted it there at Rockefeller Plaza, where of course the Rockefellers are interested and where they have been having these shows like the penguins and the seals

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all year, and they have been building up the publicity and attractiveness of it. They have guide tours through it and it was close to the N.B.C. radio broadcasting studios, from which we will draw a lot of talent.

H.M.Jr: Well, can they get an airplane in there?

Duffus: Yes. They don't have it in. It goes in on the fifteenth, the same type of plane that we had over here, right in the center of the Plaza where they had all the Mexican cactus and all. It is spotted in there and goes in the fifteenth of September. They have now one of the biggest searchlight anti-aircraft units with twelve men on it, so that any time a plane flies over New York City the crowd can gather around and they can detect a plane that is out of sight and see it when it flies over. They can pull in something, I have forgotten, it is thirty or fifty miles away, they can hear a plane from that base. It is a very, very fine show. Then I thought you might be interested on the sixteen millimeter film of "America Preferred". We had two hundred prints made of that. We talked with Chief Wilson of the Secret Service and figured out the best way to handle that, which was to turn over ten prints to him, which he in turn fastened to the end of "Know your Money", so that every time "Know your Money" is shown any place in the country, they also see "America Preferred".

Now, we are along with the retail store plan having additional copy written saying that stamps are on sale at the stores, which will be tacked on to the end of the film because right now we are starting to show it in schools and colleges and mass meetings, and the unions are starting to use it in their union meetings all over the country.

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H.M.Jr: How is the sales picture of me telling the retail fellows?

Duffus: We will have that in tomorrow afternoon, so that we can look at it Friday. Have you seen the new room downstairs?

H.M.Jr: No. Is it finished?

Duffus: The seats will be in the first of the week, and then it will be - it is all ready to use now, but the new chairs aren't in.

H.M.Jr: I will go down there.

Duffus: It is very fine.

H.M.Jr: Is it?

Duffus: We will have the other one over here, and if you are free we will see the retail film.

H.M.Jr: That all sounds good.

Graves: Is that all you had?

Duffus: That is all I had.

H.M.Jr: Mr. Callahan can review the radio situation.

Callahan: We have "America Preferred" resuming on the air Saturday night. The following Saturday night we have Suzanne Stem and under your name and in your absence last week we wired some eighteen outstanding artists. We have received sixteen replies, all favorable, all very enthusiastic.

H.M.Jr: The seventeen who have the income tax examinations?

Callahan: We have one from Rio de Janeiro. Melchoir, Josef Hoffman, out in Hollywood and says his

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knee is bad and he is awfully sorry, but he will do anything in the world. He wished he could play, but he can't. A flock of them. They are very favorable. I mean, not only accepting the invitation, but expressing thankfulness that you invited them.

H.M.Jr: What program do they go on?

Callahan: On the "America Preferred".

H.M.Jr: That Saturday?

Callahan: An artist each Saturday night.

Kuhn: That is the Deems Taylor one.

H.M.Jr: Did Deems Taylor pick these?

Callahan: He and Alfred Wallenstein, who got together and picked all these people. Then Deems Taylor and Wallenstein meet every week and discuss the music.

H.M.Jr: Who meets with them?

Callahan: Rainey. He acts in the same capacity as Mr. Monroe in the Treasury Hour. We have a new program going on Saturday, September 16, called the "Brush Creek Follies".

H.M.Jr: Brush?

Callahan: Brush Creek Follies. (Laughter)

H.M.Jr: What is this? You know, I am going to have to travel with a radio to listen to all the programs.

Callahan: That is a sort of a hill billy program which has been on the air for the past several years from Kansas City. It has been over the Columbia network. We had a man out there last week,

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and they said beginning that Saturday, that they wanted to devote the program to bonds and stamps. It is a program that appeals to farmers.

- H.M.Jr: Is it coast-to-coast?
- Callahan: Coast-to-coast. Twelve o'clock on Saturdays and I think eleven o'clock our time.
- H.M.Jr: Wonderful.
- Callahan: Of course you know we first had the Treasury Hour.
- H.M.Jr: I congratulate you on that. I showed that to the President Saturday. He was very much pleased.
- Callahan: I think that is about all. Bendix is all set. They have signed a contract with the National Broadcasting Company.
- H.M.Jr: Who is going to run that show?
- Callahan: Mr. Monroe will be in the picture. I don't know. Now, I have talked with Mr. Dietz --
- H.M.Jr: Could you come tonight and be fifteen minutes earlier, get there about a quarter past seven?
- Callahan: Yes, sir.
- H.M.Jr: I would like to talk a little bit about that before Mr. Dietz comes.
- Callahan: That is all I have.
- Graves: Mr. McCarty is Mr. Callahan's man who handles the press and magazines and publications and so on. Suppose you tell the Secretary something about what you are doing, Mr. McCarty.
- McCarty: All right, sir, Mr. Graves.

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We have a few late results, Mr. Secretary, on Baseball Defense Bond Day, which originated in the Press Section, and you have already, through Mr. Sloan's report, heard about how we set that up nationally and I think there were some of the results in there from the leading cities of the country, but since then we have gotten in more results to give us an idea of the way it went all over, and now there was scheduled that day a hundred and forty-two games over the country, professional baseball games, both the major and the minor leagues. The results show that a few of those were rained out. There were one or two - a few others we haven't heard from yet, but we have had definite word that a hundred and twenty-one of those games did see a celebration of the defense program, of Defense Bond Day, that there were bands marching, that local celebrities appeared and sat in boxes behind the home plate, and the players pledged themselves to buy bonds, all of which resulted in a good bit of attendant publicity in the newspapers and on the radio.

In New York, for instance, there were pictures in the New York Sun and the Brooklyn Eagle. There were whole columns given over to it. I just had a late report this morning that a hundred and ten stations reported that there were over five hundred announcements over Baseball Defense Bond Day on radio stations. These were good results and pleased us a good bit. Now we are hearing from the teams who were away from home that day that they would like to have a Baseball Defense Bond Day in their own home town when they go back, so we want to help them with that enthusiasm and are sending out additional transcriptions of your speech and of the introduction by High Commissioner Landis, as well

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as the literature which will be handed out by the Boy Scouts to these teams, additional ones who are coming back home and want to have their own day, and among those of course is included Washington, which unfortunately was away from home when we had the big Baseball Defense Bond Day, and the Washington club is very anxious to have their day here on September 13, which is a week from Saturday. So that will take care of our local team.

- Callahan: The Secretary might come to the game if he is in town.
- McCarty: We would like very much to have you at the game, Mr. Secretary, if you are going to be in town on that day.
- H.M.Jr: What day?
- McCarty: A week from Saturday, the thirteenth.
- H.M.Jr: I won't be here.
- McCarty: We will miss you.
- H.M.Jr: All right?
- McCarty: Just one other thing I might mention, which is the addition of several new lists of publication media, including labor publications and the shipping newspapers. We have just made out a rather comprehensive list of almost a hundred labor publications which are now going to receive material regularly as well as shopping newspapers. I don't believe there is a shopping newspaper in Washington. I know there are none in New York. But over the country there are about a hundred and eighty shopping newspapers. They are give-aways, but they are very important in some cases.
- H.M.Jr: We get one in Washington. They throw one at my front door.

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McCarty: Oh, they do have one here?

H.M.Jr: I am familiar with it.

McCarty: In Los Angeles, for instance, the Downtown Shopping News, has a million circulation. We are also going to cover the Negro press, the trade publications, the dailies, the weeklies and the foreign language groups.

H.M.Jr: I thought you might like to know, Harold, that coming down on the train Harry Hopkins said that in the eight years he has been in the Government, he thought the best public relations job that has been done by any Department is the one that you people are doing, and he said it in front of - what is the fellow from Time Magazine?

Kuhn: Belair?

H.M.Jr: He said it in front of Felix Belair, so it wasn't just something for me, and strictly in the family, the President said the worst job has been done by Harold Ickes on gasoline (Laughter).

McCarty: And Mr. Secretary, just a couple of magazines I picked up on the way over because they have just come off the press and both carry a very nice Defense Bond Message. One is Liberty, which of course has a very wide circulation, and then a woman's magazine, Harpers Bazaar, which gives us four pages, tying it up with fashions. And then there are two more pages on the other side.

H.M.Jr: This is interesting. National City Bank has something in here.

McCarty: Yes, several banks.

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H.M.Jr: It is just where they are turned down?

McCarty: There are four pages in all, sir. They have a series.

H.M.Jr: Banking people, is that the ones who take care of the girls?

McCarty: Well, that is to sell clothes and also bonds.

H.M.Jr: Does he pick the girls?

McCarty: Harpers Bazaar picks the girls.

H.M.Jr: I thought South Carolina there picked the girls. I thought he was doing a good job.

McCarty: You have probably been seeing some of the comic results that have been appearing over the country, those that have been mentioned over the reports.

H.M.Jr: Do you want this back?

McCarty: No, you may keep that. I brought it to you.

H.M.Jr: I got that comic stuff from Sloan. In that flier did you call it --

McCarty: Those were initial results. Just this morning in the Post there were two additional ones, and I believe we can be assured that they will keep up like this for an almost indefinite time, because we have the support of practically all the syndicates in the country who have gone to their artists and given them the material we prepared for them.

H.M.Jr: That helps.

McCarty: I think we can keep that up.

H.M.Jr: Good. That is good work.

Graves: Does that finish you, Mr. McCarty?

McCarty: Yes, sir.

Graves: I think you might want to hear from Mr. Edward.

H.M.Jr: I don't think you know what I mean. Come here, Edward, and look at these pictures.

Edward: I know what you are talking about, but that is twenty years ago. (Laughter)

H.M.Jr: All right.

Edward: Mr. Secretary, during the month of August we have had the wholehearted cooperation of my friends down at the Federal and the state superintendents of banks throughout the country, and with the state secretaries, and the result is that there are quite a number of other banks who are not qualified to sell bonds, but have lately qualified. The reports are not available as yet except from three of the Reserve Districts. Atlanta, Kansas City, and Dallas have sent in their reports. The others will probably be in within the next three of four days. In these three districts during the month of August forty-one additional national banks and a hundred and fifty-nine additional state banks qualified. This percentage holds good with the other nine districts. It is reasonable to predict that some seven hundred or eight hundred additional banks will qualify during August. Including these two hundred above mentioned, we now have approximately ten thousand two hundred banks qualified, and these figures do not include approximately a thousand branch banks. The head office is the only one counted in the calculation. Therefore in the banking fraternity we have about eleven thousand two hundred agents of issue for Series E Bonds.

H.M.Jr: How are we coming along with fixing up these banks to carry the E Bond without collateral?

Edward: Mr. Bell has that on his desk now. I worked on

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it last week with Mr. Batchelder and some of the fellows and we have made some suggestions for you, and I think you will probably see it in the next three or four days. I talked to Danny about it today, and he is about ready to bring it to you. We are not having a great deal of complaint from banks about putting up collateral, although the trouble is, I think, as Harold said several times, we are afraid that a good many banks are not stocking the bonds as they would if they didn't have to put up collateral, and therefore run out of bonds. For instance, out of this eleven thousand two hundred banks that have qualified, only about twenty-two hundred of them have actually pledged collateral. The other ones are just getting the sixty-five hundred dollar maximum amount of bonds and the result is that they have been running out of bonds. It probably would help some if they were allowed to have more bonds, and while we are on the subject, my recommendation, my suggestion to Mr. Batchelder was that banks might have these bonds up to the extent of - that is, insured banks, up to fifty percent of their capital in surplus with a maximum of five hundred thousand dollars to any bank, subject to some provision by the Federal. Mr. Batchelder sent out a questionnaire to the Federal Reserve Banks in all the districts asking their experience and their recommendations about this collateral. Ten out of the twelve Federal Reserve Banks recommend that we withdraw it, that we furnish the bonds without collateral.

Graves: Does that apply to all agencies or exclude building and loan, for instance?

Edward: Well, the banks, of course - the Federal Reserve didn't make any reference to the banks, but my suggestion or recommendation was that -

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Mr. Sparks was in on this conference with the building and loan people. Our recommendation was to furnish the bonds to insured banks and also to insured building and loan associations on the same basis. In other words, if they have insurance, let them all come under the blanket. Let the insurance feature be the determining factor as to whether or not they could have bonds without collateral.

Now, about the sale of E Bonds, I was talking to Mr. Sloan today and the statistics seem to indicate that August was not as good as July throughout the country, but I am very happy to tell you that I think we sold more bonds in South Carolina in August than we did in July.

H.M.Jr: Is that right?

Edward: I know my bank did, and I believe that we are actually going to sell more bonds in the state in August than in July, although the Nation shows a decrease, I think, of around twenty percent, isn't it?

Graves: Eighteen, I think, of the E Bond.

Tell the Secretary where South Carolina stands in the roll of states on this thing.

Edward: Right square on top. (Laughter).

H.M.Jr: I congratulate you.

Graves: On the basis of its proportionate share of national income.

H.M.Jr: That is wonderful.

Edward: We sold in South Carolina in July twice as many bonds as were sold in North Carolina,

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and North Carolina is twice as big a state with three or four times the wealth.

W.S.Jr: It is amazing. It shows what can be done.

Graves: That is right.

Edward: Another thing, throughout the Nation the banks have sold approximately twice as many E Bonds as the post offices have sold. South Carolina banks in July sold six times as many bonds as the post offices sold. You don't mind my bragging a little bit, do you?

W.S.Jr: I would be disappointed if you didn't. (Laughter) While we are on that, Harold, I wish you would take up with Denny Bell - I wish we could get a little more publicity on the twelve hundred dollar tax certificate. I don't think we are getting enough publicity on that. If you could pour on a little bit more publicity on the twelve hundred dollar one.

Graves: Yes, sir.

Edward: My bank is a taxpayer. I bought two hundred twelve thousand two hundred dollars worth of those things last week.

W.S.Jr: All right?

Graves: Mr. Sparks has the report of the Field Division. I think you might begin, Bob, if you don't mind, by showing the Secretary that map.

Sparks: I brought this down with the idea of leaving it with the Secretary if he would like to keep it. We hope it will be a little bit neater next week. It is the first experiment at presenting pictorially the picture of the present status.

W.S.Jr: Pennsylvania looks awfully big to me.

Graves: Kentucky and Nebraska and Iowa and Utah and

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Wyoming have people in contact with the folks in those states and we hope within the next week or so to have the beginning of an organization. there are only about, I think, six or seven states where we absolutely have done nothing.

Sparks: That is right.

Graves: And maybe in another month--

H.L.Jr: Oh, we have got to clean those up, Harold, in September. By the first of October there can't be any white states. No whites by the first of October. We have just got to. I don't want to see any white spaces by the first of October. We have just got to fix that, that is all.

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- Graves: We have had some killing luck in some of these cases. You remember I told you General Westervelt had accepted the chairmanship in Illinois. I just talked with him on the phone before I came in here and the Vice President has asked him to come to Washington to take part in all this new organization, and he wants to be excused.
- H.M.Jr: Well, no whites in October.
- Graves: I think that is reasonable.
- H.M.Jr: By the first of October.
- Graves: And we will make every effort--
- H.M.Jr: Here is New Hampshire. What is the matter with John Sullivan?
- Graves: John and I have talked about that a good many times. He has a man in mind.
- H.M.Jr: And Mrs. Ed Foley from Montgomery, Alabama. I bet you she could find somebody for you.
- Alben Barkley certainly could recommend somebody.
- Graves: That is the trouble, Senator Barkley has recommended a man in Kentucky that won't do, and we have got to struggle with that situation.
- H.M.Jr: And you ask the head of the Civil Aeronautics, Hinckley. He is an awfully good man. I bet you he could find somebody. He won't recommend anybody who won't do.
- Graves: We have a man in Utah today.
- H.M.Jr: Bob Hinckley is an awfully good man.

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- Graves: I think we will have Utah and Wyoming. I talked to Senator O'Mahoney today about Wyoming. He has recommended a man to us for administrator there. I think we will clean up those western states.
- H.M.Jr: Did you ask Senator Norris about anybody in Nebraska?
- Graves: No. We have a chairman for Nebraska, a man named McDermott, who I think is--
- Sloan: Vice president of the First National in Omaha.
- Graves: I was going to say he hasn't accepted but is expected to accept.
- H.M.Jr: Gentlemen, by September 30 you have got to clean up the United States. That is May, June, July, August, September, five months. I don't say they have all got to be red. Oh yes, that is the first color.
- Sparks: There should be some color in them.
- Graves: Well, I think we can very nearly guarantee that.
- Sparks: I think so. We will do everything under the sun.
- H.M.Jr: I have been patient. Five months. All right now, what else?
- Graves: Of course I would like to say on that point that I am the fellow, myself, that has held back on this state organization. It isn't Mr. Sparks that is in any way in default on that.
- H.M.Jr: I know. You shouldn't give me a map though, with white states on it.

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Sparks: We wanted to let you set the goal for us, Mr. Secretary. We will do everything we can to make that the zero hour for you.

H. M. Jr: September 30 is the zero hour.

Sparks: We have sent out for more detailed information on this entire picture. We have received the information from twenty-eight states so far that report that they plan a total number of five thousand and twenty-seven state and local committees in those twenty-eight states. That is the number planned. The number organized in those twenty-eight states so far is three thousand four hundred and ninety, which represents about seventy percent of the goal in those twenty-eight states. Of that three thousand four hundred ninety, seventeen hundred and sixty-seven are city committees already organized and seventeen hundred and twenty-three are county committees already organized. The total membership actually at work on these state, county, and city committees in the twenty-eight states that have reported amounts to forty-three thousand eight hundred and fifty persons on these committees in twenty-eight reporting states. We have been trying to gather factual information on the salary allotment plans as per your instructions, and we have on actual record, having reported to us so far, the names of four thousand three hundred and sixty-seven companies that have actually reported a salary allotment plan and most of them have sent copies of their plans. The total personnel in these four thousand three hundred sixty-seven companies amounts to one million four hundred nine thousand eight hundred fifty-six employees. The percentage of participation is our main headache. We are still worrying with it and doing everything possible--

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H.M.Jr: It is very few people.

Sparks: Well--

H.M.Jr: If you have got thirty-six million people at work - it is somewhere between thirty-six and forty million people that work.

Graves: If you will permit me, Bob, on that point we don't feel that we should attempt to cover any except the large and responsible employers with a payroll allotment plan sponsored by the Treasury.

H.M.Jr: Harold, as many people as we have got, God that is nothing.

Graves: I know, but it is a beginning. What I am trying to say is that we have got to leave out side this plan the persons who work in beauty parlors and stores and so on where there are only two or three or four. We can't encourage the establishment of payroll allotment plans in institutions of that kind.

H.M.Jr: I am not sure that you are right.

Graves: Well, there is the risk of default, the risk that employers will not turn in the money just as we have a certain fringe of defaulters in Social Security taxing where people don't pay it over to the Internal Revenue.

H.M.Jr: Have we got a group that is doing nothing but payrolls?

Graves: Right.

H.M.Jr: How many people are there in that group here in Washington?

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Sparks: Two.

H.M.Jr: It is not enough. You see, what you fellows forget, I am standing off a forced - a plan for forced payroll deductions by telling them they can do it this way. Here you have got two people.

Sparks: In addition to that, Mr. Secretary, we have eight field representatives, all of whom are well trained in salary allotment, but they are not concentrating their entire time on that.

H.M.Jr: Well, if you don't mind my saying it, you should have a thousand people in the field.

Sparks: Well, all of these volunteer workers are being trained in that also.

H.M.Jr: It isn't enough. I am terribly - you ought to have a thousand people going after the factories. My God! a thousand people can't cover this country. I mean, your publicity is way ahead - and you follow up on a thing - it is very disappointing. How can two people look after the business of the United States? I mean, here you have a - I don't know, the last I heard, Opacs had a thousand people here in Washington with all the business in the United States, and we have got two.

Graves: Well, Mr. Morgenthau, I don't think that is a fair analysis. Our--

H.M.Jr: Well, Harold, I don't know whether it is fair or not, but the statement is fair that you can't look after the business of the United States with two people in Washington.

Graves: I am not so sure. That is the point that I had in mind when I said what I did. Our

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reliance in this whole thing is on these state and local committees and the two people that we have specializing on this are largely people who go around and instruct our state and local committees to do this work. Mr. Sparks just told you that we have got--

Sparks: Eight field representatives.

Graves: Twenty-five thousand members of state and local--

Sparks: Forty-three thousand eight hundred and fifty.

Graves: There is the agency we have got to count on in the long run to do this job. The two people are merely going about from territory to territory advising with these state and local committees.

H.M.Jr: Now, look, I make this flat statement. Now, I have been around long enough. Whether it is fair or not, I will make it. That you haven't got one one-hundredth enough people on this payroll thing, and you will never get it done with these three thousand committees or not. Here we have been going four months and the people we have got to count on to do the saving are the factory workers, and you can't do it with eight field people paying part of their attention to this thing and two people in Washington looking after eight. We can get all the money we want, and I haven't put the pressure on you in this thing, but from now on I am going to. The people we have got to reach are in the big factories. Take a corporation like Chrysler. It would be worth while to have a half dozen people just working with Chrysler to put the thing across.

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- Graves: Well, our principle has been to induce the union people to do that work for us.
- H.M.Jr: But supposing you had - I don't know how many branches Chrysler has got. Certainly they have got a lot, all over the United States, and if there was one Treasury man with every branch and with every factory who could go to every union meeting and everything else to follow the thing up until the thing was going - you can't do it with the organization you have got and it isn't lack of money.
- Edward: Mr. Secretary, the bankers are sponsoring this payroll plan also. They are working on it.
- H.M.Jr: It isn't enough, Harold.
- Graves: Well, it isn't that we haven't had the money as you say. We have done it the way we are doing it because we have supposed that in the end that was the most effective way to work through these state and local committees instead of through salesmen that we would send around to contact the management directly, and we have avoided that.
- H.M.Jr: After four months the net result is that we have a little over a million people, I take it, with each one setting aside their savings.
- Graves: No, it isn't even that good. As I understand what Mr. Sparks has said--
- Sparks: No, that is right, it is not that good. A million four hundred is the total personnel in those companies. We don't know what the percentage of participation is.
- H.M.Jr: Then I say it is even worse than I thought it was. It has got to be better, Harold.

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- Graves: Well, I still feel that our proper approach is through these state and local committees.
- H.M.Jr: I agree with you.
- Graves: And not through paid people out of Washington.
- H.M.Jr: I don't care how you do it, but I am saying to you that if there is only a million four hundred that are signed up and of those we don't know what the percentage is, who are saving systematically each month, I am saying that after four months it isn't enough.
- Graves: That is right, I agree with you.
- H.M.Jr: And last month the national defense ran over a billion dollars and we are not keeping up with it. We have got to find some way of doing it and getting more people because if we don't I can't stand off this pressure for forced savings.
- Graves: Let me just sum up the way I feel about it. It all goes back to the slow progress that we have been making in setting up our state and county and city organizations, and once we are able to bridge that gap, I think we will make much more rapid progress.
- Sparks: I think the progress is going to be very rapid as we fill in those white spaces and as the yellows turn to blue. You will find most of these in the red states.
- H.M.Jr: Now Michigan is really organized.
- Graves: That is right.
- H.M.Jr: Can't you put in there some kind of a plan of payrolls the way you have on retail and let's

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work it out in Michigan and let's find a proper way to get Michigan, an industrial state - I suppose it is one of the most two or three highly industrial states in the country - to get it so that we can do as well on the payroll in Michigan as we have on the retail.

Sparks: I think we can.

H.M.Jr: I mean, let's concentrate on Michigan and find out. You concentrated on Michigan and you worked out a beautiful plan on retail stores. Let's take Michigan and say, we have got to get way, that if there are so many million employees working in the factories, that we will work a way out to get those people so that a high percentage of them are setting aside their savings. The thing will just be taken out of my hands. I don't want to do it the forced way, the Fascist way. I want to do it the democratic way, but if I am going to do it the democratic way, we have got to do it.

Sparks: I think we can make a demonstration in Michigan.

H.M.Jr: Let's make a demonstration in Michigan and we will get these people in factories. I have said again and again - I have asked that the list of factories in Michigan under Social Security, do we have a copy of it in Washington? I will make a bet we haven't got it.

Sparks: We haven't got the list, no.

H.M.Jr: I have asked for it for over a month, that that list, a copy of it, be here in Washington, that we get a copy of the list of the employees in Michigan, so that we can watch it and check it off.

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Sparks: Social Security lists show that there are fourteen million four hundred sixty-five thousand employees employed in companies employing eight or more employees.

H.M.Jr: Where?

Sparks: In the United States.

H.M.Jr: Get the Michigan list and get it here and let's check it off. Let's put on a campaign in Michigan on the payroll thing. What I am saying here is in the room. It mustn't get out. I must be able to talk to you people frankly. When somebody does a good job, I am delighted. If you are not doing something, we have just got to do better. Just get me a Social Security list of employees in Michigan and let's have it here and watch it and work out some way for the State of Michigan that we will get these men to saving money. Then after we solve it in Michigan, we can use it in other places. If you don't do it, take my word, they will pass some legislation whereby they will do this thing through a forced method. I don't want to do it that way. That is why I am so insistent that we do it some other way. Now, forty-three thousand people on the committee sounds lovely, but we have got to do this payroll thing, and the way to do it is to send enough people into the field to work with the unions. When I first talked about it, they were trying to settle the Ford question. They settled the Ford question. And then something else. They will have plenty to do. But they always have plenty to do. How about it, Harold?

Graves: I think your last comment is absolutely right, that our proper approach to this thing has been through the unions and that--

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H.M.Jr: Where is what's-his-name? I haven't seen him for five weeks?

Graves: He has gone back to Chicago. He has Mr. Hyatt who is working on this particular job in collaboration with Mr. Sparks' people.

H.M.Jr: I want a section set up under somebody here that I can talk to, myself, who is going to be responsible for the payroll deduction plan. I want a Mr. Smith or Mr. Brown. I want somebody.

Graves: You have that.

H.M.Jr: Well, who is it?

Graves: Mr. Touchstone.

H.M.Jr: Where is he.

Graves: He is in the field.

Sparks: In the field right now working on salary allotments.

H.M.Jr: Dammit, let's have somebody so every time I ask for him he isn't out of Washington.

Graves: That is a job that has pretty nearly got to be done out of Washington, this job of Touchstone's.

H.M.Jr: Well, I would like to talk to some fellow who is going to do the State of Michigan for me. I would like to talk to him myself.

Graves: All right.

H.M.Jr: Then let's say that whoever the man is, that is his responsibility. Who is the man--

Graves: Hyatt, I believe.

H.M.Jr: No, Houghteling. Either this is Houghteling's job or it isn't, but I haven't seen Houghteling in six weeks. He hasn't been here for six weeks. I don't know what he was doing.

Graves: He works. He was here last week.

H.M.Jr: He is not here when I am here. All right, Harold?

Graves: All right.

We will restudy that whole thing.

H.M.Jr: Give me something next week and have somebody here in the middle of the week to say, "Now this is what we are going to do in Michigan."

Graves: Fine. Does that cover your statement, Mr. Sparks?

Sparks: Yes, that does.

Graves: I think that is all, Mr. Morgenthau, unless you have something.

H.M.Jr: Now, we have got the retail thing. That is going beautifully. Now let's get the payroll thing, and get our state organizations by the first of October; and, as I say, our publicity thing is running way ahead of the rest of the stuff. Let's build that up now. We have got the eighty thousand employees in the Treasury. You can have all of them if you want to work on this thing.

Sparks: That does not include the governmental employees?

H.M.Jr: Just the Treasury alone, there are eighty

thousand employees.

Graves: Well, if you mean that in relation to this payroll allotment plan, I think that something like eighty-five percent of the Treasury employees are--

H.M.Jr: No, I meant to put a program across. I don't know how many employees we have got in Michigan, but I mean I am willing to throw the whole Treasury back of this thing to get this thing going.

Sparks: I think we can put on a very effective demonstration, one that will spread very rapidly through all the red states, and we will keep changing the colors as rapidly as possible on that so that they will all be red. I think the Secretary appreciates that, even though it is a small percentage of the total number, that the volunteer workers in the red states are responsible for most of that production.

H.M.Jr: I am an old hand at this business, and I know when a thing is going well and when it isn't, and this particular part of the thing isn't going well enough, and I think it has got to go better, that is all there is to it. I am sure it can.

Graves: Well, as I said, I think there is a worse aspect which has been developed here. Mr. Sparks gave you a figure of a million four hundred thousand people.

Sparks: That is right.

Graves: Employed by the concerns which have the plan in operation, but the number actually participating is some small percentage of that total.

H.M.Jr: You can't move a step in any office or business or street or town anywhere in Canada that you don't trip over one of their posters. I mean, you can't move anywhere and here in our own post office, when I go into the Hyde Park post office, they haven't even got a poster. Right in Hyde Park there isn't even a poster. So we just haven't scratched the surface. The President's own post office, there isn't a single poster. There was one in the back room. If you screw your neck up you can see it.

Graves: Maybe they need a new postmaster up there. It certainly is not our fault that they haven't got a poster in that post office.

H.M.Jr: Harold, if I had the time to go around and travel - and maybe I am going to have to make the time - to go around and - I would just like every place I move to see one of our posters. We have got to raise a hell of a lot of money, and we have got to mop up this extra payroll. What is the objective? They are spending all of this money, a billion dollars for defense, and it is up to the Treasury Department to mop this money up and save it so that it doesn't all go into non-defense and just make these prices go up and up and up through the scarcity if there isn't enough stuff being manufactured for the people to buy it. Our job is to mop up these savings and to keep inflation from going through the ceiling and that is what I am excited about. Now, don't let's lose sight of the fact that each person has a little job, and we have got this ten or twelve billion dollars one way or the other to raise. If we don't, we have just got to go to the banks and we just aggravate the whole situation, and it is this whole question of inflation. Now, the people have got the money, they are

- 46 -

getting it, and the roll is beginning to go in their pockets. We have got to go and get a goodly share of their earnings either first through taxes and second through their savings, and this thing, and we have been at this thing five months. We have just gotta do a better job. I know this organization can do it under Harold Graves. He has never failed me yet, and he isn't going to fail me now. All right.

## Report From Mail Order Division

September 3, 1941

This report is based on a complete picture of what has been accomplished in the Mail Order Division of the Defense Savings Staff since its inception last spring.

The chart of activities includes:

(1) Regular Purchasers - those who, as the result of previous solicitation, are buying at regular intervals. To this list (approximately 100,000 at the present time), we are starting this month to send a special letter and three order forms, asking their cooperation in bringing the bonds to the attention of others.

(2) Customers - all those who have bought but who haven't agreed to buy regularly. To this list (approximately 2,000,000 as of July 31st), we are sending a letter urging adoption of the Regular Purchase Plan, a colorful folder and a Regular Purchase order form. These start going out this Friday, September 5th.

(3) Prospects - large investors - taken from the Customer and I. R. files. To this list (375,000 corporations, partnerships, associations, etc.), we have just sent a special mailing consisting of a letter, order form and folder featuring F and G bonds.

(4) Prospects - smaller investors. These are the I. R. names (approximately 4,874,000 as of July 31st) that we are testing - in a variety of different ways - in order to find the formula that will produce maximum results.

Before we discuss the results of our testing to date, let me raise one point that seems to me to be vitally important. In one sense, this mail order campaign - including all of our mail selling efforts - is different from practically all others. In any commercial mail order business, the product is available only by mail and results are measured in but two ways - the mail orders that come back and the repeat business that follows.

In this mail order campaign of ours, results should be determined by:

- (1) The number of people who are induced to send their orders direct.
- (2) The amount of money received in relation to the cost of getting it.
- (3) The amount of potential repeat business that becomes available at a very low selling cost.
- (4) Equally important - the educational work done on the entire list.

Thus, from Test Series No. 1 for instance, which went out June 21st, it should be remembered that in addition to getting 300 people to buy over \$140,000 worth of bonds at a cost of 85/100th of 1 percent, the mailing called on 94,256 other people - told them the entire Savings Bond story, and provided one more link in the chain of publicity and advertising being used to raise money for national defense.

From Series One, relative returns mean more than total orders or dollars received. We put these ten tests in the mail, with existing material, to find out things and from that standpoint, they accomplished their purpose.

We learned, for instance, that it was safe for us to circularize on Defense Savings Staff stationery; that a mailing on E bonds was as good, if not slightly better, than a mailing on all three bonds; that there was an extremely small demand for F bonds. We also learned that if our best test had been sent to the entire list, the selling cost would have been down to 73 cents for each \$100 worth of bonds sold.

That should represent a maximum selling cost for future mailings, since none of the assemblies in Series No. 1 contained specifically prepared mail order material, and had the further disadvantage of being sent out during one of the poorest mail selling seasons of the entire year.

From Series Two, which went into the mails July 19th, we are likewise getting some useful information. While returns are incomplete, it seems safe to conclude that the best test, both from the stand-

point of orders and dollars received, will be an E mailing - thus confirming what we discovered in Series No. 1. We have also learned that with all other factors being equal, our new folder "How To Buy A Share In America" is outpulling the blue and white Defense folder used in the first tests; that the State of Massachusetts produces twice as many orders as the State of Michigan; that a combination of letter, folder and order form is more productive than a card, folder and order form.

From Series No. Three, which went into the mail last Saturday, August 30th, we will get a comparison between the pulling power of I. R. names with incomes over \$5,000, incomes under \$5,000 and a mixture of the two. This list check-up is being made in California, Georgia and Maryland. Also being tested are several new letters; an advertising message on the envelope versus a plain window envelope; and, as another confirmation, the pulling power of E bonds versus all three.

This third series is going out at a very favorable time. In a comparatively short while it should give us an indication of the returns that can be expected from the approximately 2,000,000 new over \$5,000 names that have just been put on plates, as compared with the greater number of under \$5,000 names that are available if it is found desirable to circularize them.

...

Eileen Buckley



1. MOUNTAIN  
 2. PLATEAU  
 3. DESERT  
 4. PLAIN

**CLEARTYPE  
 MUNICIPAL CITIES MAP  
 OF THE  
 UNITED STATES**

Scale: 1:500,000  
 Date: 1960  
 Author: [illegible]  
 [Additional text and a scale bar are present here.]

September 3, 1941  
4:50 p.m.

HMJr: I'm all right, Breck.

Breckenbridge  
Long:

Well, Henry, I thought maybe you could take an interest in this over in your department and see if you couldn't - let me present the thing to you briefly.

We're troubled in this country by a lot of German propaganda films.

HMJr: Yeah.

L: They're some of the very bad things floating around here.

HMJr: Yeah.

L: There's one, "The War On The Western Front".....

HMJr: Yeah, I know about it.

L: And there are three or four more. The tendency was just to scare our people.....

HMJr: Yeah.

L: .....and subdue them.....

HMJr: Yeah.

L: .....and we've been trying every way to get some action to either take these films or to intercept, and.....

HMJr: Well, let me interrupt you, Breck, because I know all about this.

L: Well.....

HMJr: Any that come in - have been coming in now for some time - we don't let them get out any more.

L: Yeah.

- 2 -

HMJr: But those which are out, we can't do a thing about it.

L: Well, I wondered if you couldn't by a stretch of interpretation - you do, now, hold those from coming in by taking their bills of lading.

HMJr: Yeah. Well, we.....

L: You freeze the bills of lading, in other words.

HMJr: Well, I don't know how we do it; but those that come in now, they just never get on the market.

L: That's right.

HMJr: But those which are out - I've been all through that, and there isn't a thing that we can do unless the Attorney General can think up something.

L: Uh huh. It just occurred to me - we had a meeting here about it this afternoon.....

HMJr: Yeah.

L: .....that this UFA thing, they come to UFA - U - F - A - and UFA is simply a wholly-owned subsidiary of this German parent company.....

HMJr: Uh huh.

L: Which, in itself, is fostered and subsidized by the German government.

HMJr: I'm a hundred percent with you, and if anybody - if the Attorney General can tell me how to do it - I'd love to do it.

L: Uh huh.

HMJr: I can promise you that for over a month now there have been no more coming in.

- 3 -

L: Yes.

HMJr: The last time we showed one we had the Attorney General here. It was a picture called, "Bismarck".

L: Uh huh.

HMJr: And we all voted on it and the amusing thing, Mrs. Biddle said, "Don't let it come in," and Biddle said, "Let it come in," to be different.

L: (Laughs)

HMJr: We out-voted him.

L: Yeah.

HMJr: But we haven't let any come in. It's a month or six weeks, now.

L: Yes, I knew that. But these other old things are still marching around.

HMJr: We can't do a damn thing about it.

L: Uh huh. Well, I just thought that maybe you - it hadn't come to your personal attention.

HMJr: No, I happen to know all about it, but.....

L: Well, then I won't bother you with it or take any more of your time.

HMJr: .....but I can promise you that no more will come in.

L: Yeah. Yeah. Well, we're - have been very much interested and have been wrestling with it for a month or six weeks here, and I just thought that it hadn't come to your personal attention; but you've had it, why that's all I got to say.

HMJr: Thank you, but call me any time.

L: All right, Henry, thank you.

THE WHITE HOUSE  
WASHINGTON

September 3, 1941

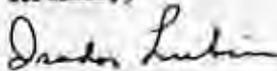
My dear Mr. Secretary:

My friend Mr. Guthrie was not among those mentioned in the newspaper clipping that you sent me yesterday.

I have made inquiry as to the basis of the newspaper report, and I find that it is in reference to an attempt to get some order out of the chaos that has prevailed in the Army trading posts. It appears that there is no uniformity of prices even for standard products. I have been told that in some instances the prices charged for nationally-advertised products at Army posts are higher than those charged in private downtown shops. Mr. Guthrie has been seeking to get some system of centralized buying so that variations in prices from post to post may be eliminated. Even cigarette prices vary from post to post.

The new setup, as I understand it, will make it possible for each trading post to buy any place it wishes on condition that the wholesale prices it must pay to local jobbers are no higher than the prices quoted to the central buying office in New York. At the same time, a definite mark-up is to be provided. In this way, there will be a top limit to the prices that can be charged to soldiers at the Army posts. Moreover, in the case of some nationally-advertised brands, the proposed procedure will make it possible to sell certain commodities at prices below those which prevail in private stores.

Cordially,

  
Isador Lubin

The Honorable  
The Secretary of the Treasury  
Washington, D. C.

September 2, 1941

Dear Mr. Lubin:

What about this story? Is it  
a reflection on your friend about whom  
you spoke to me?

Sincerely yours,

*H. M. Jr.*

Honorable Isador Lubin,  
The White House,  
Washington, D.C.

By Messenger

*4:05 pm  
Singer*

## ARMY EXCHANGES CENTRALIZE BUYING

War Dept. to Set Up Office  
Here After Report 'Arbitrary  
Objections' Hit Program

### PLAN PRICE AGREEMENTS

Each Post Unit Will Take Orders  
From Manufacturers—Use Basis  
of These Quotations

The War Department is centralizing purchasing operations Monday for Army post exchanges at 111 Eighth Avenue, it is learned yesterday.

This action follows a report published in The New York Times last Sunday to the effect that "arbitrary objections" of a part of high-ranking Army officials were threatening to disrupt the centralized administration of post exchanges.

The purchasing department which will be under direct control of Colonel Frank Mansfield, will make price agreements with manufacturers on thousands of articles sold on the exchanges. Individual post exchanges then will order on the basis of such price agreements.

Accounting, personnel and administrative offices of the Army's post exchange program will remain in Washington. It is noted that the post exchange program is an annual business of approximately \$250,000,000 a year.

Colonel Mansfield will be assisted by Captain John H. Kresge, formerly connected with the S. S. Kresge Company, and Captain Robert E. Cooper, formerly with Montgomery Ward.

Grocery interests were mentioned yesterday by the Army officials. The food men had become restless about what they described as unnecessary delay in getting the post exchange program operating. They had complained that remaining Army officials had overlooked suggestions advanced by business men who had gone to Washington specifically to help in getting the post exchange program organized and operating.

September 3, 1941

Dear Mr. Mackenzie:

In the last few crowded years I have met many, and become quite intimate with some, splendid personalities representing your government. There were few, however, whom I came to like more, whose talents and services in the cause of Britain I estimated higher, and whose loss I could feel more deeply, than that of Arthur Purvis.

Though you and I have never met, we have in common the bond of the loss of one whom both of us called our friend. I wish you to know how profoundly I appreciated your thoughtfulness in writing to me.

Yours sincerely,

(Signed) A. Morgenthau, Jr.

Mr. Moir Mackenzie  
21 Tothill Street  
London, S.W.1

JG:eh

Mr. P.  
- to Clippel  
cc - Miss Channing

FEDERATION OF BRITISH INDUSTRIES

346

TELEGRAMS:  
INDUSTRY, PARL. LONDON.

TELEPHONES:  
WHITEHALL 8711.  
(10 Lines)

DIRECTOR:  
GUY LOCOCK, C.M.G.  
GENERAL SECRETARY:  
D. L. WALKER.



21, TOTHILL STREET,

LONDON, S.W.1.

YOUR REF.

OUR REF.

18th August, 1941.

Henry Morgenthau, Esq.,  
Secretary of the Treasury,  
Washington, D.C.,  
U.S.A.

*Dear Mr. Morgenthau*

We have never met, but I feel compelled to write to you to express my deep and real sympathy with you at the passing of your friend Arthur Purvis. I can well believe that his death, and in such tragic circumstances, must have been a terrible blow to you. I think you will be glad to know that when he lunched with me just a couple of days after his arrival here he spoke of you in glowing and grateful terms for your consistently wise council and help.

From a National point of view his many friendships in both countries, and his immense understanding of our mutual problems, would seem to render him irreplaceable.

As one who held him in deep regard may I venture to say that I share with you your sorrow at the death of our friend.

*Yours faithfully  
Gwior MacKenzie.*

Willard Hotel,  
Washington, D.C.,

3rd September, 1941.

Dear Mr. Secretary,

I have your letter of September 2nd stating that you have designated Dr. H.D. White to be the Treasury's liaison officer for all matters of lend-lease arrangements and of the British dollar position.

I shall be glad to arrange for all communications and enquiries on these subjects intended for Treasury consideration to be channeled through him in the future.

Believe me,

Dear Mr. Secretary,

Yours sincerely,

*F. Phillips*

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

SEP 2 1941

My dear Sir Frederick:

I have designated Mr. E. D. White to be the Treasury's liaison officer for all matters of Lend-Lease arrangements and of the British dollar position. In future, therefore, I would appreciate it if all communications and inquiries on these subjects intended for Treasury consideration were channeled through him.

Sincerely yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury.

Sir Frederick Phillips,  
Under Secretary of the British Treasury,  
British Supply Council in North America,  
Willard Hotel,  
Washington, D. C.

File to Mr. Thompson.

HW:ash  
9/11/41

gov Secy's office

TREASURY DEPARTMENT  
INTER OFFICE COMMUNICATION

DATE September 3, 1941

TO Secretary Morgenthau  
FROM H. D. White

Subject: American airplanes in the United Kingdom

1. Colonel Roy A. Dunn, one of General Arnold's men, has just returned to the U.S., after making an intensive inquiry as to the number of unused American airplanes in Britain. He told Coe that:

- a. He had himself counted 1,200 unused American planes, a large number of which were still in crates.
- b. He knows the places where they are.
- c. Various explanations were given him as to why they were not in use --lack of personnel, lack of proper equipment, absence of spare parts, and the desire to re-test on the spot the planes received.

Two additional reasons may be (1) the influence of vested airplane contractors' interests in England, and (2) the suspicion of high British air officials of certain kinds of American equipment.

2. Stacy May, of O.P.M., also made some inquiries. The British gave him the following figures:

Tomahawks in R.A.F.....	456
Tomahawks "arrived" but "not been delivered" to R. A. F.....	283
Other American planes "arrived" but "not been delivered" to R. A. F.....	About 500

There are other American planes in "storage reserve" and these may make up the 1,200 Dunn spoke about. Mr. May is "satisfied he has the full story and that, considering the value of P-40, the British are using it as well as they can".

3. Coe stated that because you omitted reference to the question of American airplanes in your recent cabled instructions to him, he is not following up that subject. You may want to contact the two men for the full story. (May is due back in the U.S. if he is not already here).

(Coe to Secretary, August 18)

## TREASURY DEPARTMENT

## INTER OFFICE COMMUNICATION

DATE September 3, 1941

TO Secretary Morgenthau

FROM Mr. Kamarck

Subject: British Article on the Flying Fortress

The following are excerpts from an article in the London Times' "Trade and Engineering" periodical, August 1941 issue.

## The Fortress 1

"The official British name for the B 17 G, known in the United States as the Flying Fortress, is to be the Fortress 1. The original order of 20 machines has now been completed and delivered, and as these giant bombers have proved to be every bit as good as their American manufacturers claimed, it is hoped that many more will be flown over soon. Further deliveries have been promised under the Lease and Lend Act, and it is expected that these will be a later and improved version, the B 17 E. ...If there is any criticism which could be made of the Fortresses which have so far been sent over for the use of the R.A.F. it is that, like almost every other American machine, they are under-armed.

"The writer recently had the opportunity of inspecting the last of the original deliveries at a Ministry of Aircraft Production depot, where they were being overhauled before being sent on to an operational squadron of the R.A.F. Bomber Command. ...The Fortress's ceiling is put at 41,000 ft. when carrying 39,000 lb., but even though it is known to be an excellent performer at high altitude, this may be rather an over-statement.

"Major Carl Brandt, senior test pilot of Boeings, came over in one of the first machines delivered across the Atlantic to give the British authorities the benefit of his advice and to instruct test pilots in flying them. The Fortress is already extremely popular with the R.A.F. crews, for, having been constructed originally for civil purposes, it is roomy and extremely comfortable. ...The test pilot at this M.A.P. depot -- an R.A.F. officer with a long experience of bomber aircraft -- told the writer that the Fortress was the best aeroplane that he had ever flown. It was completely free from vices and, when once one had got accustomed to the instrument panels, it was quite easy to fly, in spite of its great size.

"An interesting development at this depot is the establishment of special engine shops for handling the three main types of American motors -- the Allison, Pratt and Whitney, and Wright Cyclone. One shop has been set aside exclusively for the assembly, overhaul, and reassembly of Allison engines, which are now being used by the R.A.F. in great numbers in the Tomahawk fighters which have given such a fine account of themselves in the Middle East and elsewhere. This move should greatly simplify the problem of the maintenance of American aircraft and engines in this country, which, in the past, has given no small amount of trouble."

## TREASURY DEPARTMENT

## INTER OFFICE COMMUNICATION

DATE September 3, 1941

TO Secretary Morgenthau  
FROM H. D. White

Subject: Post-War Policy of Free Trade

Many British officials are uncertain whether the United States realizes the implications of its request that Britain go along with a post-war policy of free trade. They question whether the U.S. Government is going to be willing to lower its tariffs, make the necessary internal economic adjustments, and grant the large credits necessary to enable the rest of the world to abandon exchange and trade controls.

Some British Treasury officials have said to Coe "that they would be all for free trade if after the war England, and other countries, have sufficient foreign exchange income to pay for the goods they will need". Many fear, however, that England will not be able to abandon exchange controls after the war and that a return to "free trade" as it used to be conceived is not going to take place.

Mr. Baxter's section of the Ministry of Post-War Planning is tackling as their first job the problem of freer trade, because of the President's request for a statement of policy. They are in a quandary; they do not wish to displease the United States, and yet they do not know that they will be able to abandon foreign exchange control.

The Times editorial of August 18 on the Roosevelt-Churchill conversation (which Coe enclosed) manifests a real doubt as to whether what the United States seems to be asking can really be achieved. Coe suggests that the U.S. Treasury should earmark some men for full time study of these problems.

(Coe to Secretary, August 18)

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MURRAY HILL 2-1100

*Emergency Committee for Zionist Affairs*

41 EAST 46th STREET  
ROOM 1121  
NEW YORK CITY

September 3, 1941

Hon. Henry Morgenthau  
Secretary of the Treasury  
U.S. Treasury Department  
Washington, D.C.

My dear Mr. Morgenthau:

I am writing you following the conversation I had with your secretary Mrs. Klotz. Since it is uncertain whether you will be able to see me tomorrow, Thursday, I am taking the liberty of enclosing copy of a memorandum which we have submitted to Under Secretary Welles, following several conversations which we had with him. In the last interview he assured me of his readiness to approach the British Government through Mr. Winant, in order to receive the desired assurance that nothing is being done or will be done at this time to affect the status of Palestine.

We have had no word on the subject from Mr. Welles since then. In the meantime, however, we have received from Dr. Weizmann certain documents which confirm our supposition that negotiations are being carried on with the Arabs which directly and indirectly affect Palestine. There are matters in this connection which I would prefer to discuss with you orally, and will be glad to have the opportunity of doing so the latter part of next week.

With deep appreciation of your helpful interest, I am

Very sincerely yours,  
*Esmanuel Neumann*  
Esmanuel Neumann

Enc.

*Mr. Neumann  
for the EC  
9-11-41 3:30 pm*

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August 7, 1941

Hon. Sumner Welles  
Under Secretary of State  
Washington, D. C.

Dear Mr. Secretary:

Supplementing the recent meeting which Mr. Emanuel Neumann on behalf of the Emergency Committee for Zionist Affairs had with you, I have the pleasure of submitting herewith the memorandum which he undertook to submit on our behalf. We hold ourselves in readiness for a conference with you touching this problem, should you find it necessary further to discuss the matter with us.

I am, dear, dear Mr. Secretary, with most hearty greetings

Faithfully yours,

Stephen S. Wise

MEMORANDUM SUBMITTED TO UNDER SECRETARY OF STATE  
THE HONORABLE SUMNER WELLES

354-A

BY THE EMERGENCY COMMITTEE FOR ZIONIST AFFAIRS

1. It has been generally assumed that British policy with regard to Palestine would undergo no important modification during the progress of the war. In Zionist circles it was hoped that no further steps would be taken toward implementing the White Paper of 1939 and it was believed that there would certainly be no basic change in the status of Palestine or of the Palestine Mandate.

2. A recent address delivered by the Secretary of State for Foreign Affairs, Mr. Anthony Eden, made specific reference to a coming change in the status of Syria and Lebanon and promised support by the British Government for a scheme of federation in the Middle East as yet undefined.

Dr. Stephen S. Wise and Dr. Nahum Goldmann conferred with you shortly thereafter, and you were kind enough to state that in your view it was extremely improbable that the British Government would take any steps involving the status of Palestine either by the inclusion of Palestine in a federation or otherwise, without prior consultation with the Government of the United States; and furthermore, that if proposals affecting the status of Palestine or of the Jewish National Home were forthcoming, the American Government would accord the representatives of American Zionism adequate opportunity to present their views before taking any position on such questions.

We take this occasion to express our profound appreciation of these statements made by you at the time to our representatives.

3. Since the interview referred to took place, signs have been multiplying that the question of new political dispositions in the Middle East have been occupying the attention of important British circles following the termination of the Syrian campaign. There is in our considered judgment reason to believe that the possibility of effecting a political reorganization in the Middle East is being considered in British official quarters. This has given rise to a certain apprehension lest under the pressure of war and of military developments in that region, steps may be taken or commitments made which involve the status of Palestine and of the Jewish National Home, in a manner and direction we can not foresee or judge at this distance. Such steps or commitments, if made either publicly or

privately, may conceivably lead to the result that the Mandate for Palestine would be materially affected at a time when neither the League of Nations nor its permanent Mandates Commission are in a position to function. A further consequence would be that such international settlement as may be expected to take place at the end of the war may be prejudged by such commitments or by the creation of accomplished facts.

4. We would therefore respectfully suggest that it would be most helpful if the American Government would elicit from the British Government authentic information on ~~make~~ this subject as well as an assurance that it does not intend to carry on negotiations or make commitments involving a change in the legal and political status of Palestine or a derogation of the position of the Jewish National Home, whether by promoting a union between Palestine and other territories, or otherwise; and that no steps will be taken without previous consultation with the government of the United States.

We wish to record our gratitude to you for so kindly offering to act promptly in this matter, and to express the hope that we may be informed of the result in due course.

TREASURY DEPARTMENT

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INTER-OFFICE COMMUNICATION

DATE September 3, 1941

TO Secretary Morgenthau

FROM Mr. Cochran

The following table presents a breakdown of our silver purchases by sources:

Sources of Silver Purchased Under  
the Silver Purchase Act -- 1941

<u>Country of Origin</u>	<u>Jan.-June</u>	<u>July</u>	<u>August</u>	<u>Jan.-August</u>
(In thousands of dollars)				
<u>New Production Silver</u>				
Argentina	\$ 201	\$ --	\$ 80	\$ 281
Canada	1,263	420	420	2,103
Honduras	659	79	147	885
Java	59	180	--	239
Peru	2,014	307	280	2,601
Not Designated*	3,428	333	538	4,299
Total New Prod.	<u>\$7,624</u>	<u>\$1,319</u>	<u>\$1,465</u>	<u>\$10,408</u>
<u>Other Silver</u>				
China	\$ 282	--	--	\$ 282
Japan	918	--	--	918
Mexico	175	--	--	175
Not Designated*	280	\$ 210	\$ 201	691
Total Other	<u>\$1,655</u>	<u>\$ 210</u>	<u>\$ 201</u>	<u>\$ 2,066</u>
<u>Grand Total</u>	<u>\$9,279</u>	<u>\$1,529</u>	<u>\$1,666</u>	<u>\$12,474</u>

\*A large part of the "Not Designated" silver is believed to represent imports from Mexico. For comparison purposes, total silver imports into the U.S. from Mexico are given below, according to type of silver:

	<u>Jan.-June</u>	<u>July</u>	<u>August</u>	<u>Jan.-August</u>
(In thousands of dollars)				
New Production	\$2,798	\$ 577	\$ 198	\$ 3,573
Other (refined)	<u>9,875</u>	<u>2,148</u>	<u>2,005</u>	<u>14,028</u>
Total	\$12,673	\$2,725	\$2,203	\$17,601

*B. M. F.*

September 3, 1941.

Dear Mr. Director:

This will acknowledge receipt of your letter of August 27, on the subject of measures for the protection of places and facilities essential to the National defense and asking that I name a responsible person in the Treasury Department who may confer with Brigadier General Gasser, of your office, on the matter.

I designate Herbert E. Gaston, Assistant Secretary of the Treasury, as my representative with respect to the matters of which you write. Mr. Gaston will shortly write you with respect to the questions raised in your letter.

Sincerely yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury.

Honorable F. H. LaGuardia,  
U. S. Director Civilian Defense,  
Washington, D.C.

*File to Mr. Gaston  
cc - Miss Chauncey*

MINUTES OF THE ECONOMIC DEFENSE BOARD SEPTEMBER 3, 1941

Present at the meeting were:

Assistant Secretary of State Dean Acheson,  
Assistant Secretary of State Brewsteridge  
Long, Under Secretary of War Robert P.  
Patterson, Assistant Secretary of the Navy  
Adlai Stevenson, Mr. Harry White represented  
the Secretary of the Treasury, Mr. L. A.  
Roehler represented the Secretary of Agriculture,  
and Mr. Will Clayton represented the Secretary  
of Commerce.

Mr. L. P. Hickell, War Relocation Commission also  
attended.

Assistant Secretary of State Long reported that the State  
Department and the Inter-Departmental committee, had been studying  
coffee. South American countries using coffee have progressively  
raised coffee prices. It was reported by the Assistant Secretary  
of State that Columbia has set fifteen different prices on coffee  
recently; each new price being higher than the last. He stated that  
Mr. Henderson, of Office of Production Management, has filed recom-  
mendations regarding coffee prices. Assistant Secretary of State  
Acheson said that Mr. Paul Daniels has given much study to coffee.  
The Vice President asked Mr. Laurence Duggan, of the State Depart-  
ment, and Mr. L. A. Roehler, of the Department of Agriculture, to  
consult with Mr. Hamm, of the Office of Production Management, and  
Mr. Paul Daniels, and report back to the Defense Board.

The Vice President stated that hereafter any problems will  
be handled in their preliminary stages outside of formal Board meet-  
ings, recommendations of the staff being presented to the Economic  
Defense Board. He said that the Economic Defense Board now has an  
office at Kew Apartments, telephone number 5090, Extension 1000.

Mr. Will Clayton stated that an exporter is compelled to go  
through six different agencies before he knows whether he can export  
materials of this class. It was his opinion that in view of the  
President's policy that after the Supply Priorities and Allocations  
Board has made a ruling, there should be no need for special export  
licenses. The Vice President said that he is informed by Mr.  
Donald Nelson, Executive Director of the Supply Priorities and

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Allocations Board, that 10,000 export licenses have been granted, that there are 20,000 export licenses pending, and several thousand have been denied. There is a bottleneck because of slowness in deciding upon export licenses, in Mr. Nelson's opinion. Mr. Nelson says that he will clear the whole situation up in one week's time. Mr. Will Clayton said that many exports to South America are not subject to priority and that it should not be necessary for South American countries to procure export licenses for such commodities. The Vice President asked that Mr. Clayton discuss this matter with Mr. Donald Nelson.

Under Secretary of War Patterson stated that Russia has made such large demands upon the United States for materials, that we will not be able to help South American countries substantially. Mr. Clayton stated that one-third of our copper comes from South America and that we must return some copper and other materials to South America. The Vice President asked Mr. Clayton and Mr. Acheson to discuss this situation with Mr. Donald Nelson.

The Vice President asked Assistant Secretary of State Long for a report on the final destination of oil which is being shipped from Port Arthur, Texas to Spain. Assistant Secretary of State Long stated that the report that much of this oil is going to Germany and Italy is probably incorrect, but that the State Department is not yet ready to file its report and recommendation.

The Vice President stated that his information is that little, if any, goods are now being shipped to Japan. Assistant Secretary of State Acheson stated that some goods are going from the Philippines to Japan. Mr. Harry White said that it may be advisable to adopt preclusive selling as well as preclusive buying. It was his recommendation that we should learn exactly what goods are being sold by Japan to the Philippines and South America and that we should under sell Japan on such materials. Mr. Will Clayton stated that Japan is buying much less from South America now and is not selling any goods in South America due to the freezing of Japanese funds in the United States and the failure of Japan to get raw materials. Mr. Clayton stated that Federal Loan Agency has a \$8,000,000 fund for the purpose of de-Germanizing South American air lines. He said that quartz crystals, platinum, and industrial diamonds and mica are being shipped from South America to Italy by airplane and that this air service should be stopped.

BY THE PRESIDENT OF THE UNITED STATES OF AMERICA

## A PROCLAMATION

WHEREAS the act of Congress entitled "An act to facilitate the construction, extension, or completion of interstate petroleum pipe lines related to national defense, and to promote interstate commerce", approved July 30, 1941 (Public Law 197 - 77th Congress), vests in the President certain powers relating to the construction, extension, completion, operation, and maintenance of interstate pipe lines related to national defense.

NOW, THEREFORE, I, FRANKLIN D. ROOSEVELT, President of the United States of America, under and by virtue of the authority vested in me by sections 2 and 3 of said act of July 30, 1941, do hereby find and proclaim (1) that it is necessary for national defense purposes that there be constructed and completed a pipe line system for the transportation and distribution of petroleum and petroleum products moving in interstate commerce, the route for which is generally indicated on a map which is on file in the Office of the Petroleum Coordinator for National Defense, detailed survey maps of which shall be of record in the said office, commencing at Port St. Joe, Florida, and extending in a northerly direction through the States of Florida and Georgia, and into Tennessee to a point on the Tennessee River at or in the vicinity of Chattanooga, Tennessee, (2) that Southeastern Pipe Line Company, a private corporation organized under the laws of the State of Delaware, has commenced the work necessary for the construction of such a pipe line system, and has partially constructed the same and represents that it is prepared to complete said pipe line system, and (3) that it is necessary for the purposes of construction, completion, operation, and maintenance of said pipe line system that the Southeastern Pipe Line Company have the right to acquire, by the exercise of the right of eminent domain as provided in the aforesaid act, along the route and between the points hereinbefore identified, (a) such parcels of land or any interests therein, not in excess of 100 acres in each separate parcel, for the location of its storage tanks, pumping stations, delivery facilities, and other facilities in connection therewith, and (b) easements and rights of way, not in excess of 100 feet in width, for the construction, completion, operation, maintenance and removal of the pipe lines, including right of access thereto over adjoining lands: Provided, That such right of eminent domain be exercised by the Southeastern Pipe Line Company for the aforesaid purposes prior to June 30, 1943.

The pipe line hereinbefore identified shall be constructed, completed, operated, and maintained subject to such terms and conditions as the President may hereafter from time to time prescribe as necessary for national defense purposes.

IN WITNESS WHEREOF, I have hereunto set my hand and caused the seal of the United States to be affixed.

DONE at the City of Washington this third day of September  
in the year of our Lord nineteen  
hundred and forty-one, and of the  
(SEAL) Independence of the United States  
of America the one hundred and  
sixty-sixth.

FRANKLIN D. ROOSEVELT

By the President:

CORDELL HULL,

Secretary of State.

FOR THE PRESS

IMMEDIATE RELEASE

FOR THE PRESS

SEPTEMBER 3, 1941

Announcement was made today of appointment by the President of the membership of the Mission to Russia as follows:

Chairman, W. AVERELL HARRIMAN, now serving as the President's Special Representative in London on Material Aid to the British Empire.

MAJOR GENERAL JAMES H. BURNS, Executive Officer, Division of Defense Aid Reports associated with Harry L. Hopkins. General Burns has served with distinction in the Ordnance Department of the Army.

MAJOR GENERAL GEORGE H. BRETT, Chief of Air Corps, at present on a special Mission to Great Britain and the Middle East in connection with deliveries of American aircraft.

ADMIRAL WILLIAM HARRISON STANDLEY, U. S. NAVY, former Chief of Naval Operations, 1933-37. Admiral Standley was a member of the Delegation of the United States to the General Disarmament Conference held in London, 1934, and a delegate on the part of the United States to the London Naval Conference of 1935.

WILLIAM L. BATT, Deputy Director, Production Division, Office of Production Management. Chairman, Business Advisory Council for the Department of Commerce. Mr. Batt is President of S.M.F. Industries, Inc., and Chairman of the Board, American Management Association.

The Mission will join with a similarly constituted British Mission under the Chairmanship of Lord Beaverbrook for a conference in Moscow with the Russian Government regarding the supplying to Russia by the United States and Great Britain of munitions, raw materials, and other supplies needed by Russia for her defense against German aggression.

The holding of this conference was agreed to between the President and the prime Minister at their recent meeting at sea.

## TREASURY DEPARTMENT

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## INTER-OFFICE COMMUNICATION

DATE September 3, 1941

TO Secretary Morgenthau  
FROM Mr. Cochran

STABILIZATION AGREEMENTS

China: On July 14, 1937 the Treasury entered into an agreement with the Central Bank of China to purchase yuan up to a total of \$50,000,000 U.S. currency. The agreement has been renewed each six months and now expires December 31, 1941. At present we hold 65,000,000 yuan, whose book dollar value is \$19,112,500, and against which \$19,379,015.65 in gold is held at the Federal Reserve Bank of New York as collateral. The rate of interest is 1/2% above the current rediscount rate of the Federal Reserve Bank of New York.

Brazil: On July 15, 1937, the Treasury entered into an agreement with the United States of Brazil, which expires on July 15, 1942. We agreed to purchase milreis up to a total value of \$60,000,000, with Brazil leaving on deposit in New York gold collateral to guarantee the repurchase of the milreis by Brazil. The rate of interest is 1/2 of 1% above the current rediscount rate of the Federal Reserve Bank of New York. There have been transactions under this arrangement, but at present we are holding no milreis. This agreement also provides for the sale of up to a maximum amount of \$60,000,000 in gold by the United States to be held under earmark in our vaults for the account of Brazil. This agreement was modified on September 2, 1938, to permit Brazil to ship gold from abroad to be held in this earmarked account. Up to August 30, 1941, \$29,465,770.90 in gold had been sold by us to Brazil and \$11,532,765.19 had been shipped by Brazil to New York to be held under earmark.

Argentina: On January 1, 1941, the Treasury entered into an agreement with the Banco Central de la Republica Argentina and the Government of Argentina. Under this agreement we undertake to purchase Argentine pesos up to the equivalent of \$50,000,000 U.S. currency. No collateral is required. The interest rate is fixed at 1-1/2%. The agreement comes into operation and effect upon ratification and confirmation by Argentine of the authority under its constitution and laws to enter into this agreement. Up to the present time the foregoing conditions have not been met and the agreement is inoperative. The agreement was drafted to expire on June 30, 1941. An extension of the agreement has also been drafted, but cannot be made effective until the agreement itself becomes operative.

China: On April 1, 1941, the Treasury entered into an agreement with the National Government of the Republic of China and the Central Bank of China. This calls for the purchase by the Treasury of Chinese yuan up to the equivalent of \$50,000,000 U.S. currency. No collateral is required. The agreement expires June 30, 1942. Interest at the rate of 1-1/2%. China has not yet called for the \$50,000,000. The Chinese-American-British Stabilisation Board in China, on which Mr. A. Manuel Fox is the American representative, did, however, begin to operate in the middle of August. The Chinese Government banks have deposited with the Federal Reserve Bank of New York their contribution of \$20,000,000 to the joint Stabilisation Fund.

Mexico: An agreement with the Government of the Republic of Mexico and the Banco de Mexico is practically ready for signature. This involves purchases of Mexican pesos by the United States up to the equivalent of \$40,000,000 U.S. currency. There is no collateral. The rate of interest is at 1-1/2%. The repurchase clause with Mexico gives that country 180 days' notice and then an additional 180 days within which to repurchase. This is a generous departure from our usual 30 days' notice. The Department of State expects its related negotiations with Mexico to be consummated in time for the signing of the Stabilization agreement before September 15. The Treasury is also to agree to purchase up to 6,000,000 ounces of silver monthly from Mexico, under an arrangement similar to that which we have with Canada.

Colombia: The Ambassador of Colombia has recently returned from his country to which he went a few weeks ago with a draft Stabilization agreement with the Stabilization Fund of the Government of Colombia, the Banco de la Republica, Bogota, Colombia, and the Government of the Republic of Colombia, under which the United States would buy Colombian pesos up to the equivalent of \$3,000,000 U.S. currency. No collateral is involved. The interest rate would be 1-1/2%. We should have further discussions with the Colombian Ambassador shortly.

Ecuador: When the Ecuadorian Minister of Finance visited Washington in August he discussed with the Secretary, and subsequently with the Secretary's assistants, the question of a Stabilization agreement which might provide as much as \$5,000,000 U.S. currency. It is not believed that more than perhaps half of such a sum could at all be justified. The Department of State has requested that we continue negotiations with the Ecuadorian Ambassador.

Bolivia: We have promised the State Department that we would consider a Bolivian request for monetary assistance.

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BRITISH EMBASSY,

WASHINGTON, D. C.,

September 3rd, 1941.

With the Compliments of Mr. W.

Ritchie

Copy of letter dated September  
3rd to Mr. Dean Acheson

Mr. Merle Cochran,  
U. S. Treasury Department,  
Washington, D.C.

Copy:new 9/4/41

BRITISH EMBASSY,

WASHINGTON, D.C.,

September 3rd, 1941.

SAFE HAND

Dear Mr. Acheson,

The following is the text of a statement made by Mr. Eden in the House of Commons on August 6th:-

"The Honorable members will remember that about a week ago I announced certain freezing measures, which had been instituted by the United States, the Netherlands and the British Empire against Japan as a result of the Japanese seizure of bases in French Indo-China. Those freezing measures are not, as seemed to be thought by some Honourable members in the debate, framed so as to permit transactions which are not expressly forbidden. On the contrary the operation is the reverse. They automatically forbid all transactions except those which are expressly permitted. As the House will understand, I cannot now disclose the details of the manner in which this policy is to be applied but there has been throughout closest collaboration and frankest discussion between His Majesty's Government at home, in the Dominions, in India, Burma and in the Colonies, and the Governments of the United States and the Netherlands; and the two latter Governments have furnished us with full particulars and with comprehensive information of their actions. The same collaboration is continuing regarding the operation of these measures as was in evidence in former days. The House will understand that it is bound to take a little time to exchange the views and information which are necessary for common understanding of such a far-reaching experiment as freezing orders will present. But that work is now practically completed. There is one assurance I would like to give the House; these steps were not lightly taken. The Freezing order was seriously intended and it will be seriously executed."

Mr. Dean Acheson,  
Assistant Secretary of State,  
State Department,  
Washington, D. C.

HFB:WR;TMI

cc to Mr. Cochran

- 2 -

I am sorry you have not had this before, but I have only just received it myself.

I am sending a copy of this letter to Mr. Cochran for his information.

Yours sincerely,

(Sgd) Noel F. Hall

Copy:mew 9/4/41

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DEPARTMENT OF STATE  
WASHINGTON

September 3, 1941

In reply refer to  
EA 840.51 Frozen Credits/3254

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury and transmits a copy of despatch mailed August 13, 1941 from the American Consulate General in Hong Kong concerning the reaction in Hong Kong to recent freezing orders and the placing of the Colony of Hong Kong in the sterling bloc.

Enclosure:

Mentioned above.

VOLUNTARY  
(Supplementing radio message No. 293 of August 6, 4 p.m.)

CONFIDENTIAL

HONG KONG REACTION TO RECENT FREEZING ORDERS  
AND THE PLACING OF THE COLONY IN THE  
STERLING BLOC

From:

John H. Bruins  
American Consul

Hong Kong	Date of Completion:	August 11, 1941
	Date of Mailing:	August 13, 1941

Approved:

Addison E. Southard  
American Consul General

COPY

1. Bank "Runs" of Short Duration:

On the two business days following the announcement of the freezing of Chinese assets, local Chinese withdrew considerable sums in local currency from their local bank accounts. This small "run" soon stopped, and there was nothing approaching a panic. Hong Kong banks were not embarrassed by this withdrawal, as nearly all of them are overburdened with deposits which are difficult to loan out advantageously.

2. British Control Orders Slow in Arriving:

The principal complaint of most bankers is the slowness in arrival of the official British orders regulating both the "freezing" and the entry of Hong Kong into the sterling bloc. It is pointed out that such regulations have been in force in Singapore for many months, and that all the details should have been immediately available here. American banks in Hong Kong have also received conflicting telegrams from their New York headquarters, and the atmosphere of uncertainty prevails. This is regarded as an annoyance and as an added business risk, which will probably be removed in the course of a week or two.

- 2 -

### 3. Uncertain Status of Bills Payable:

The principal difficulty is the status of bills payable. Most of these are in Chinese names. The purchase of such bills is an important part of banking business here. Telegraphic inquiries to New York by the local banks have brought equivocal replies. The National City Bank continues to buy them. The Chase Bank continues to handle them in small amounts. The American Express Company has declined to handle them until the situation is clarified. The Chase Bank reports that some such bills sent to New York early in July, long before the present orders were issued, have been refused payment. It has been requested by its New York headquarters to supply a full report on the number and amounts of such bills now in transit.

### 4. Difficulties of Shanghai Arbitrage:

Local banks used to sell Shanghai dollars to importers, and covered by sending foreign currency equivalent to Shanghai. Under the new "sterling bloc" regulations, it is apparently impossible to send out such foreign currency remittances. Such transactions

occur

- 3 -

occur mainly in connection with textile imports from Shanghai (at least such part of the business as has not fallen into Japanese hands), local importers thus requiring Shanghai dollars in payment. Before negotiating business of this type, banks have satisfied themselves that the business is being carried on by a bona fide Chungking-sponsored firm. Some bankers are inclined to attribute the weakness in Shanghai currency in recent days to the aforementioned lack of demand for it, attributable in turn to the inability of supplying cover. The manager of the American Express Company stated confidentially to-day that he had just been authorized to supply the sterling cover from their London office to Shanghai. He explains this by the fact that every such transaction requires exhibition of bills of lading and thus represents goods coming into the Colony and also by the fact that reimbursement comes to him in the form of Hong Kong dollars which are a controlled currency. The above is another example of non-uniformity in practice due to conflicting orders under which the banks are at present operating.

Uneven

Copy:wec:9-3-41

5. Uneven Spots in Administration:

There are numerous instances of inconvenience and annoyance. The manager of the Chase Bank mentioned two instances. Last April his New York headquarters recommended the transfer of all U. S. dollar accounts in Hong Kong to New York, in view of the uncertain situation in the Far East. This was carried out. Many of these accounts were in the names of Chinese persons. Some difficulty has been experienced in obtaining release of money for their children's education in the United States, although it is understood provision has been made under a general license for such living expenses. The second is an instance of a Chinese person having a loan of about US\$1,000,000 against about two million dollars worth of securities. The market having been favorable, securities to the value of about \$1,000,000 were sold in New York to liquidate the loan, but cannot now be transferred, and interest must still be paid on the loan. It is also understood that quasi-Chinese Government institutions such as the Postal Bank and the Central Trust of China have not been granted general licenses.

6. Americans Obligated to Report All Holdings:

British subjects were formerly compelled to register their holdings abroad. Recent Hong Kong regulations have extended this obligation to all nationalities. Thus, American citizens now in Hong Kong are obligated to report to the British authorities all of their holdings, even in the United States, and to offer them to the British authorities at the convenience of the latter against payment in sterling or local currency. Thus far, there has been no compulsion exercised in regard to holdings of local Americans in the United States. However, this matter has already caused one American millionaire to leave the Colony suddenly, and has also made impossible the operation of American brokerage offices here, dealing in American securities. There are two such viz: Levy Bros. and Swan, Culbertson & Frits.

7. Colony Reconciled to Trade Curtailment:

Special permits from the local currency control authorities are required before any personal remittances abroad may be made. For example, nearly all men make constant remittances to their wives who have been evacuated,

and

and each such transaction now calls for a permit. Thus far they have been freely issued. On the other hand, business remittances are closely scrutinized, and it appears inevitable that the inclusion of the Colony in the "sterling bloc" will result in a serious curtailment of trade.

800

800  
JHB:bp

**Distribution:**

In quintuplicate to the  
Department (by air mail);  
Hectograph copy to the  
Department;  
Copy to Embassy, Chungking;  
Copy to Embassy, London;  
Copy to Consulate General,  
Shanghai.

Sources of Information:

Interviews with Hong Kong  
bankers as noted in the  
text;

Recent Hong Kong Government  
Financial Regulations;  
United States Executive  
Order 8389 as amended by  
Executive Orders No. 8785  
and No. 8832. Also gener-  
al licenses 54 to 69 issued  
under these Executive Orders.

C  
O  
P  
YDepartment of State  
Washington

September 3, 1941.

In reply refer to  
EA

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury and encloses five copies of a paraphrase of telegram No. 444, dated September 1, 1941, 5 p.m., from the American Consulate at Manila, Philippine Islands, transmitting a message for the Secretary of the Treasury from Mr. A. Manuel Fox.

## Enclosure:

From Consulate, Manila,  
No. 444, September 1,  
1941.

Copy:mew 9/3/41

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Consulate, Manila, Philippine Islands

DATE: September 1, 1941, 5 p.m.

NO.: 444

S T R I C T L Y   C O N F I D E N T I A L .

THE FOLLOWING IS FOR THE SECRETARY OF THE TREASURY  
FROM FOX.

"Business as usual" continues to be the attitude in Shanghai. Every effort is being made by both the Board and myself to impress upon licensed banks that an emergency exists. The only bank that is cooperating is the Hong Kong & Shanghai Bank. A few others, such as American banks, give lip service cooperating only for a day or two.

Drastic action with respect to license No. 59 may be necessary if the losses of the Board are to be kept within reasonable limits. As immediate action, it is suggested that licensed banks be threatened and warned of the withdrawal of its privileges under this license.

As an alternative, I could recommend to the Board the lowering of an official rate. However, from our many discussions of the subject, I am confident that this would have a bad psychological effect in China where, in view of rumors of peace, they are especially sensitive at the present time.

With respect

With respect to license No. 59, threat and warning would have an effect, especially if it were done publicly, in Chungking. The suggested warning and possibly even more drastic action would be an essential step before the lowering of the official rate by the Board should it prove to be necessary to make such a reduction.

With regard to telegram No. 206: The subject of imports into China is covered in some detail in my memorandum, United States trade with China urgently needs to be closer controlled. I decidedly recommend either the revoking of general licenses Nos. 58 and 64, except for trade via Bangkok, or the adopting of the system of export licenses lines of the order of August 25 of the British Board of Trade. The Department is in the best position to make the final choice in this matter.

I have just learned from Noble of the Export Control of the Philippines that there has been a loosening of control of United States exports to Shanghai instead of a tightening as it appears that it is comparatively easy to get licenses approved in Shanghai. Taylor had already been instructed to prepare the material on the questions which were raised in telegram No. 206. This information will be forwarded at the earliest opportunity to the Department.

It is most desirable to have family remittances reach the Board automatically. It is necessary that each important

area

area have a point of centralization. In the United States the authorized channel could be the efficient Bank of China. After local consultations, I am suggesting that the Central Bank of China be the point of centralization in the Philippines. (It was recommended previously that the Philippine Bank of Communications have this position.)

Should the Central Bank of China, which already has a deposit account with the Philippine Bank of Communications, open a deposit account with the China Banking Corporation in Manila, all remittances could funnel through the Central Bank of China there. I am urging the Government of China to approve this procedure rather than that which was previously recommended. I am also making arrangement through the office of the High Commissioner along these lines.

Would it be possible for action to be taken when the remittances are centralized in the U.S. to provide that these be made at the official rate of the Board? Should this be so, parallel action in the Philippines could easily be taken.

There is great opportunity at the present time for economic survey and recommendations provided the Government of China is made aware of the definite interest and the support of Washington. There are many urgent questions on which there is a good chance of some remedial actions.

It is proposed that native talent be used; however, direction and supervision is needed in such matters.

4

It would be appreciated if Adler could be made available to me for work in Hong Kong and China. At the present time Adler is in Manila. Since Adler has previously worked with Far Eastern problems and freezing, he would be of great help.

The relation of the Board to the Agency is important. A Frankenstein is created by the letters of April 25 in providing for the agency to which all foreign exchange from remittances and exports may accrue, with parallel powers to the Board. There is convincing proof that an attempt is being made to take full advantage of the latitude of the provisions of April 25.

At the present time, the Agency is being set up as a highly political collection. All members of the Board are greatly worried by the highly political complexion of the Agency as it is now being set up. A clash between the Agency and the Board will inevitably develop -- leading to an ugly situation for the Department -- if nothing is done.

It is therefore recommended strongly that the Department consider this--preferably in collaboration with the British. Hall-Patch is quite disturbed. I know that he would welcome such action which would advise the Board and the Government of China that:

(a) It is the opinion of the Treasury General Counsel that the Board should be set up by Executive Yuan decree, dated August 12, especially as the Agency has been so set up and as no difficulty is experienced in China in predating decrees.

-5-

(b) It is the considered opinion of the Department that the Agency should concentrate on policy matters and that the exchange operations should be reserved to the Board particularly because of its technical competency and compactness. To save face for the Agency it could be suggested that it pass a resolution that the Board handle all of the exchange transactions.

Please stress the urgent need for action since the Chinese members have already been requested to return to Chungking to attend the initial meeting of the Agency but were advised by me to await my return there.

This is the end of the message.

HICKOK  
SAYRE

EA:PAK

Copy:bj:9-3-41

## PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Consulate, Saigon, French Indochina

DATE: September 3, 1941, 5 P.M.

NO.: 88

A complaint has been made to this Consulate by the Inspector General of the Bank of Indochina in regard to the proceeds of a shipment of wolfram which amounts to \$15,289.13. This was credited to the blocked account of the French-American Banking Corporation on May 28, 1941. The Inspector General also complained that the Treasury had refused to allow the transfer of the credit under reference to "special account A". This action, the Inspector General claims, is in violation of the license which was issued in accordance with Executive Order No. 8389 on the seventh of March.

This Consulate would be glad to learn if and (if when) disposition (if is) (if made) of the proceeds in question in order that this Consulate may use this information for its own guidance in future dealings with the Bank of Indochina.

This message was sent to Cavite in order that it might be repeated to the Department for its information.

BROWNE

(NOTE: A repetition of the garbled groups has been requested. Should the correction be other than that interpreted, the proper persons will be notified.)

KAIPAK 840.61 Frozen Credits/3341

TREASURY DEPARTMENT

384

INTER-OFFICE COMMUNICATION

For Miss Chauncy

DATE September 3, 1941

TO Secretary Morgenthau

FROM Mr. Cochran

**CONFIDENTIAL**

Registered sterling transactions of the reporting banks were as follows:

Sold to commercial concerns	£ 79,000
Purchased from commercial concerns	£122,000

Open market sterling held steady at 4.03-1/2, and there were no reported transactions.

In New York, closing quotations for the foreign currencies listed below were as follows:

Canadian dollar	10-9/16% discount
Argentine peso (free)	.2374
Brazilian milreis (free)	.0505
Colombian peso	.5800
Mexican peso	.2070
Venezuelan bolivar	.2750
Uruguayan peso (free)	.4425
Cuban peso	1/2% discount

In the unofficial exchange market in Shanghai, the yuan advanced 1/16¢ to 4-13/16¢. The sterling-dollar cross rate worked out to 4.04, off 1-3/8¢.

There were no gold transactions consummated by us today.

The Federal Reserve Bank of New York reported that the Bank of Canada shipped \$2,759,000 in gold from Canada to the Federal for account of the Government of Canada, for sale to the New York Assay Office.

We were informed that the Bombay gold price on August 30 was equivalent to \$34.14, or 12¢ higher than the quotation for August 23. Silver was priced at the equivalent of 44.70¢, up 1/8¢.

The prices fixed in London for spot and forward silver remained unchanged at 23-1/2d and 23-7/16d respectively. The U.S. equivalents were 42.67¢ and 42.55¢.

The Treasury's purchase price for foreign silver was unchanged at 35¢. Handy and Harman's settlement price for foreign silver was also unchanged at 34-3/4¢.

## CONFIDENTIAL

- 2 -

We made two purchases of new production silver amounting to 100,000 ounces under the Silver Purchase Act. This silver, which was bought for forward delivery, came from various foreign countries.

The report of August 27, received from the Federal Reserve Bank of New York, giving foreign exchange positions of banks and bankers in its district, revealed that the total position of all countries was short the equivalent of \$4,898,000, an increase of \$127,000 in the short position since August 20. Net changes were as follows:

Country	Short Position August 20	Short Position August 27	Change in Short Position*
England**	\$ 38,000 (Long)	\$ 166,000	+ \$204,000
Europe	2,769,000	2,700,000	- 69,000
Canada	154,000 (Long)	100,000 (Long)	+ 54,000
Latin America	112,000	36,000 (Long)	- 148,000
Japan	71,000	116,000	+ 45,000
Other Asia	2,019,000	2,091,000	+ 72,000
All others	8,000 (Long)	39,000 (Long)	- 31,000
Total	\$4,771,000	\$4,898,000	+ \$127,000

\*Plus sign (+) indicates increase in short position, or decrease in long position.  
Minus sign(-) indicates decrease in short position, or increase in long position.

\*\*Combined position in registered and open market sterling.

BRITISH EMBASSY,  
WASHINGTON.

September 3rd, 1941.

PERSONAL AND SECRET.

Dear Mr. Secretary,

I enclose herein for your personal and secret information a copy of the latest report received from London on the military situation.

Believe me,

Dear Mr. Secretary,

Very sincerely yours,

*R. J. Campbell*

The Honourable

Henry Morgenthau, Jr.,

United States Treasury,

Washington, D.C.

TELEGRAM FROM LONDON DATED SEPTEMBER 1st, 1941.

August 30th/31st.

8 1/2 tons of high explosives and nearly 1,000 incendiaries dropped Cherbourg. Many bursts seen in docks area.

2. 51 Blenheims bombed industrial buildings Lille, aerodrome in Brittany, and shipyards near Rouen. Fortress from 55,000 ft. dropped bombs in the centre of Bremen. Fighters escorting Blenheims destroyed 1 enemy fighter. We lost 2 fighters.

3. Night of 31st/September 1st.  
Nearly 200 aircraft despatched; targets included Cologne and Essen; 7 missing.

4. Night of August 30th/31st.  
9 Wellingtons attacked Tripoli.  
One ship hit and set on fire.

5. Malta. August 30th/31st.  
Five torpedo bombers attacked 1200 ton enemy merchant vessel near Lampedusa. One hit scored left ship listing heavily.

6. German Air Force. Aug. 31st/Sept. 1st.  
93 aircraft operating of which 55 crossed coast. One destroyed by night fighters. Main concentration on Hull and neighbouring district. Some damage to house property and some casualties.

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MILITARY INTELLIGENCE DIVISION  
WAR DEPARTMENT  
Washington, September 3, 1941

TENTATIVE LESSONS BULLETIN  
No. 153  
G-2/2657-235

NOTICE

The information contained in this series of bulletins will be restricted to items from official sources which are reasonably confirmed. The lessons necessarily are tentative and in no sense mature studies.

This document is being given an approved distribution, and no additional copies are available in the Military Intelligence Division. For provisions governing its reproduction, see Letter TAG 350.05 (9-19-40) M-B-M.

THROUGH SUN AND SANDSTORM TO SOLJUMSOURCE

This bulletin is based on a translation of an article which was written by a German war correspondent. The article was published in April in the Voelkischer Beobachter, a Berlin daily newspaper.

Intended propagandistic effects should not be overlooked.

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THROUGH SUN AND SANDSTORM TO SOLLUM

The men of a reconnaissance detachment were the first German soldiers to reach the Libyan-Egyptian frontier and to occupy the Egyptian frontier station of Sollum. They first set foot on African territory in the middle of February, and scarcely eight weeks later they were a full 1700 kilometers - reckoning only the distance on the coast road - away from their starting point, Tripoli. And in those hundreds of kilometers were embraced the most difficult marches under the greatest privation; days and nights of wakefulness and fighting, of defense, of attack and reconnaissance; sandstorms and the scorching heat of the sun - an accomplishment of men and materiel so incredible that it is almost indescribable.

When they reached Africa, the men knew nothing of the desert; they knew the land only from books and stories. But they saw it with their own eyes, and they lived it on a march which took them from Tripoli to Sirte in less than two days. That trek alone was an achievement for men and machines, and it showed what could be accomplished, even under completely unfamiliar circumstances, by will power and intelligent leadership; for even the command of the German African Corps had not expected that the detachment could travel to Sirte in such an amazingly short time.

Just behind Sirte lay the main battle line of the Italians. The detachment took but one day's rest and then pushed forward again, across the Italians' main battle line and on to Nofilia, 130 kilometers from Sirte.

At Nofilia the detachment was detailed to hold the enemy, to reconnoitre in his direction, and to throw him back if he should make an attempt to attack the German position. Many were the tasks that had to be performed, tasks which were fitting for a reconnaissance detachment. All branches of service represented in the detachment were well supplied with work. The armored reconnaissance cars; the infantrymen; the crews of accompanying guns; the pioneers; the antitank guns; the intelligence personnel; the motorcycle rifleman companies; the transport crew; the red cross personnel; all felt the load. Day and night everyone was prepared and on guard.

Three weeks went by. Slowly the front was pushed farther forward into the region of Arco del Fileni. Again and again reconnaissance troops approached the enemy in an effort to ascertain the strength of opposing forces. Twice these reconnaissance troops came in contact with the enemy. The first clash between German and English troops in Africa took place on the morning of February 24, 1941, southeast of Agedabia. The skirmish was costly for the English, who

lost both men and material. While German troops thus faced the enemy, they familiarized themselves with the desert, in which, as they well knew, they soon would have to fight a battle unlike any they had ever fought before.

In the gray of dawn on March 24, exactly a month to the day after the first meeting of German and English strength, the attack rolled on El Aghella, which a weak British force had occupied by surprise. Frontally, and with a flanking movement, the Germans advanced on El Aghella and took it. The well-mined terrain in front of the position delayed, but did not stop the attack; and once again the reconnaissance detachment could rest, only to advance 1,000 kilometers less than two weeks afterwards.

El Brega was the next goal. After a stubborn resistance, it was taken on the dawn of March 31, by sections of the reconnaissance detachment in conjunction with tanks, Stukas, and machine gun units. From then on the advance against the enemy continued at a pace that had hitherto been thought impossible in desert country. After securing the right flank of the German troops at El Brega, and then capturing Agedabia on April 2 and securing the left flank, the reconnaissance detachment began its really great period with the advance on Bengasi.

Would Bengasi be defended? Was it the strong position that the English said it was? Would not the enemy do its utmost to hold this port? Over the road to Bengasi the convoy rolled, and above it, like great invisible question marks, hovered those thoughts. As always, the scout troops were in the van to guard against surprise. To the side of the road, deserted refueling camps and ruined vehicles gave their little pictures of the great war. Kilometer after kilometer ground away under wheel. Ever searching, the men's eyes looked out across the countryside and ahead and down the road. Over there—ain't that an English tank behind that truck that's shot to pieces? Cautiously the vanguard stalked closer. There was no movement; it looked suspicious. The young lieutenant colonel, automatic pistol in hand, walked up to the scene; his eyes widened. In a tent, sleeping quietly and peacefully as if there were no Germans, were three Tommies. "Morning boys," the voice of the lieutenant colonel started the three up out of their sleep. One reached quickly for his pistol, but let it fall when he saw the threatening barrel of the automatic pistol in front of him.

The flanking guard stretched far out into the desert on both sides of the road; Bengasi was approached on a broad front. Night turned to morning - Bengasi was in German hands. It could hardly be believed. The city, the possession of which meant so much, had fallen into German hands without a struggle. And just as the Germans could scarcely believe it, the Italians were beside themselves with happiness

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and joy; they prepared a tremendous reception for their allies. All the cares and anxieties, the privations and sacrifices that had been stored up, were changed in a flash to one great transport of joy.

The march continued, and the position was made secure beyond Bengasi. After that 170 kilometer jump from Agedabia to Bengasi, there was a two-hour rest. The soldiers stretched out under palm trees, ate and refreshed themselves, showed each other the first bite of booty, and scrubbed some of the dirt out of their sweat-covered faces. And from there, too, the radio message went out that Bengasi had fallen. Suddenly, out of a clear sky, came a good luck omen. General Rommel, who "is always everywhere, and always in the front," as one of the men once said, stood in the midst of the officers and men of the reconnaissance detachment.

A burning heat covered the land as the detachment turned toward the east, away from the coast road and into the desert. March, march, march, came the order; do not lose sight of the enemy again; stay right on his heels. The commander of the reconnaissance detachment knew the deep significance of his mission, and he fulfilled that mission so well, that, at the victorious conclusion of this great advance all the way to the Egyptian border, the Führer and Commander in Chief bestowed upon him the Knight's Cross of the Order of the Iron Cross for his brilliant leadership and personal bravery. Included in this reward to Lieutenant Colonel Baron von Wechmar, of course, was recognition of the splendid achievement and the exemplary fighting spirit of his detachment.

No longer was the road smooth under the vehicles' wheels; sand and stones alone paved their way. Above, was only the sun and thick dust. Mouths grew dry and tongues too lazy to speak - even if they could speak in that furnace of hell. But onward, ever onward, pushed the detachment. Benina was reached and passed. Suddenly word came from the van - machine gun nests and strong fortifications are on the heights, and tanks are in the hollow. Already the enemy artillery was flashing; everything halted. In a trice the detachment was broken up, the artillery was brought into position, and everything humanly possible was done to meet the sudden fire. The decision was reached immediately - attack; tanks forward! A dense, raging curtain fire confronted the attacking tanks, but they paid no attention to it, nor to the mine fields that had to be crossed and the toll those mines demanded. The tanks rolled toward the hill fortification and fought their way through it, but a broad antitank trench brought them to a halt, and they had to turn back. The enemy immediately began an infantry counterattack, but German motorcycle riflemen were ready, and they threw themselves against the counterattackers. Pioneers were already breaking paths through the thick mine fields. Artillery on both sides thundered unceasingly. Step by step the men worked their

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way toward the enemy position; the machine gun nests which had not already been disposed of by the tanks, were mopped up by the infantrymen. Under cover of darkness, the men reached the antitank trench; there they held their position all night. Forgotten were dust and weariness; only the law of war applied, and that permits but one thought - to fight.

While the battle was raging, pioneers were working feverishly to repair explosion craters in the winding road that lead to Fort Regima; the vehicles had to have a clear road during the planned attack. Slowly the din of fighting died down; alert and watchful, the Germans waited. Only the cries of the wounded interrupted the still of the night. At dawn Nazi troops came out of their cover and stalked closer to the fort. A terrific tension hung over the men. No shots fired? Confound it, why don't they fire? Cautiously the men felt their way forward; the top seemed an eternity away to them, but they finally reached it. The fort had been evacuated in the night, and only a part of the garrison was still there. That part surrendered, and numerous prisoners were taken.

Once again the desert swallowed up the long column, now marching in convoy. Through the sand it moved, across El Abiar and then straight toward El Mechili. No longer were there roads; the compass was the only road sign, and the vehicle tachometers the only kilometer stones.

Suddenly one evening the vanguard reported that some 40 enemy tanks were approaching in a frontal attack and that approximately the same number were coming from the north. It looked bad, very bad. Eighty tanks were not going to prove an easy foe. The only redeeming feature was that they apparently had little heart for attack. At any rate they hesitated. Swiftly the column turned and made for a commanding height to the rear; then it formed a defense front against the superior tank forces of the English. The detachment took up a hedgehog formation, so that it could instantly meet attacks from any side; but nothing happened.

In the early afternoon a reconnaissance patrol surprised and captured a British gasoline convoy on its way to the tanks with necessary fuel. As it took little thought to realize that if the English tanks had no more gasoline, they could not stay in battle very much longer, it was decided to break through the line of tanks. The mission had to be accomplished; no more time could be lost. At twilight the detachment started on its mad night march through the desolate wasteland of gorges, wadies, and sand. It could only travel at an average of ten, or at most fifteen, kilometers per hour; the vehicles had almost to feel their way forward, as they bounced from side to side on the rocky ground. In the morning the riddle was solved.

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Many of the tanks were standing in the desert; some were still with crews, some deserted. Their gasoline supply had run out, and they lay helpless at the mercy of the Germans. Without much delay the journey was continued, until a mine field just in front of Mechili barred the advance and made a rather long stop necessary.

But the desert had not shown all of her obstacles yet. A heavy sandstorm started up and the march became a torture. Despite everything, however, the detachment reached Mechili at the very moment that other German units were taking the village. The catch made there was wonderful. Not only were six generals and 2000 men taken prisoner and 14 German prisoners set free, but immeasurable material booty was also captured. From tanks to golf clubs, from serious weapons to the tools of the Englishman's sports, from whiskey to fruit preserves - everything was there. Think what that meant to troops which had not had anything hot to eat for five days; for men who had had to exist on a half liter of water per day and who had perhaps even poured that in the radiator of their conveyance simply because the motor needed it even more than did the thirsty men!

In spite of the tremendous exertions of the days gone by, no rest could be given the troops. The advance on Tobruk by the coast road had begun. The attempt to veer around the enemy far to the south had failed because of the insurmountable difficulties of the terrain.

In the meantime, units of the machine gun battalion had gained possession of a route over which Tobruk could be passed to the south. To be sure, that meant marching more than 70 kilometers in the worst part of the desert, but that made no difference - the main thing was that it could be done at all. The second great desert trek began. The way lead across Acroma, and soon English reconnaissance tanks bobbed up. But the antitank defense was alert, and two of them were put out of commission. The others retreated; but from a distance they could still direct the fire of a battery on the marching detachment. A bigger loop had to be made to the southwest to avoid that battery.

Everything comes to an end sooner or later. At noonday the detachment marched on past El Adem and then once more through the worst kind of sandy desert. A sigh of relief went up in the ranks when the wheels once more struck the coast road. The detachment was now behind Tobruk's own defenses and could take up the task of advancing past Bardia to the Libyan-Egyptian frontier. Very cautiously, on the night of April 11, it set out along the coast road toward Bardia. To the right and left of the road British reconnaissance cars and tanks were still wandering about in the countryside. Just as the first German vehicles approached the city, the harbor road was blown up and fire poured out of the magazines, signs that the English had just withdrawn. Considerable booty in materiel and supplies fell into the hands

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of the Germans, who quickly occupied Bardia and extended their defenses to the heights in back of the city. Then the giant hedgehog, with weapons bristling, stood watch, while reconnaissance troops scouted in the direction of Sollum. Unceasingly, British low flying planes and bombers raked the advancing detachment, but with little success. What German soldiers have once attained they do not give up, no matter how hard the enemy may resist. On the evening of April 12, the message came from the advance units: "6:40; Libyan-Egyptian border crossed and Sollum occupied," - there was great joy.

For eight weeks this reconnaissance detachment had been on African soil. Always facing the enemy, never at rest; waking and fighting, attacking and defending itself; the desert had become its home.

He alone who has felt the hot breath of the desert, who has endured to the end the torture of thirst without water, who has, in near desperation, reached for the iron ration, can know what it means to fight in the desert. Only he who for hours and days in the Ghibli has sat in a conveyance or stretched out in a tent with a handkerchief over mouth and nose, who, with a few comrades, has pushed in sheer desperation, and to exhaustion, a vehicle stuck fast in the sand, who has looked in vain on the smooth flat surface of the desert for cover from a low flying plane, knows what African fighting is.

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RESTRICTED

G-2/2657-220; No. 483 M.I.D., W.D. 11:00 A.M., September 3, 1941

SITUATION REPORTI. Eastern Theater.

Ground: The German drive from Gomel southeastward made slight progress on August 31st. Another German Armored Division succeeded in reaching the Briansk—Kiev railroad to the northeast of Voronezh. To the south of Berezna, progress was also made. In this sector German infantry units are approaching the Desna River. The six German bridgeheads east of the Dnepr River were not enlarged on August 31st.

No definite information has been received with regard to operations on the Yartsevo—Roslavl—Bryansk front, although Russian counterattacks appear to be continuing at various points along this line.

German advances continued in the Leningrad sector on the 31st. A German column advancing northeastward from Tosno reached the Neva River at Ivanoykskoye, a town to the northeast of Kolpino. Farther east a German combat group, advancing northeastward from Chudowa down the Volchov, has reached the railroad station of Myslowe on the Leningrad—Jaroslavl railroad.

To the southwest of Leningrad, German forces advancing from Kingisepp have captured the village of Bisguinzy. Unofficial reports from Berlin state that the German advance has actually reached the area just south of Krasnoyeselo.

Air: The Italian communiques reported German bombings of large forces of Russian aircraft concentrated on the Kiev—Gomel—Smolensk line.

II. Western Theater.

Air: British planes made night raids on Berlin, starting a large number of fires, and also operated over northern central and southwestern Germany. German activity was reported over airports in the Midlands and ports on the British east coast.

III. Middle Eastern Theater.

Ground: Little of importance.

Air: British air activity has been strong recently against Tripoli, Bengazi, Bardia and Gambut. Fleet Air Arm claims bombed aircraft at the Italian bases of Gherbini and Comiso, Sicily. Malta was raided by Italian planes and British ground forces are reported by the Italians to have been machine-gunned in the Jarabub oasis.

RESTRICTED

London, Filed: 4:37 p.m., September 3, 1941.

1. British Air Activity over the Continent.

a. Night of September 1-2. 43 tons of HE, including one 4000 pound bomb, and 5000 incendiaries were dropped on Cologne. 10 tons of HE were also dropped on secondary targets.

b. Day of September 2. A total of 401 fighters were employed as follows: 116 in the protection of shipping, 55 on interception patrols, 196 on offensive missions and 34 on special operations. Off Stavanger, 3 Beauforts attacked 3 motor vessels, claiming hits by torpedoes on one motor vessel of 7000 tons and an escort vessel. Both vessels were believed sunk. These aircraft were engaged by 3 German He-109's. 3 direct hits on a 4000 ton motor vessel off the Belgian coast were claimed in an attack by 3 Heinkels with fighter escort. 2 B-17's, which had been dispatched to Duisburg and Hamburg, abandoned their missions because of bad weather. A third B-17 attacked Bremen from 30000 feet. No German aircraft opposed this attack. One of the bombs dropped was observed to burst in the center of the city.

c. Night of September 2-3. A total of 199 bombers were dispatched as follows: 125 to Frankfurt, 32 Hampdens, 7 Halifax, 6 Stirlings and 4 Manchester to Berlin, 10 to Ostend, and 15 on sea mining off the Frisian Islands. Although atmospheric conditions over the targets were good, there was widespread fog over the British Isles and most aircraft were compelled to land away from their base bases.

2. German Air Activity over Britain.

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- 3-
- a. Day of September 1. 15 Bomber-reconnaissance aircraft, 15 long range bombers and 3 fighters were used.
  - b. Night of September 1-2. 5 mine layers, 5 reconnaissance aircraft and 25 long range bombers were employed.
  - c. Day of September 2. Defensive fighter patrols were maintained in the area of Calais.
  - d. Night of September 2-3. Defensive night fighters patrolled in the area of Cherbourg. Offensive night fighters operated over East Anglia and Lincolnshire. Long range bombers were active over St. Abb's Head and Whitby.

### 3. Aircraft Losses Reported.

a. British losses. During the day of September 2, no fighters were lost. 1 torpedo carrying Beaufighter failed to return. 1 Heinkel was lost by anti-aircraft fire off the Belgian coast. Bomber losses during the night of September 2-3 were as follows: Frankfurt raid, 4 lost, 5 crashed in England, the crew of one of which was killed; Berlin raid, 2 Hampdens, 2 Halifax and 1 Manchester lost; and sea mining mission, 2 lost.

b. Axis losses. On September 2, British fighters shot down 2 Me-109's. Another Me-109 was destroyed in the engagement with Beaufighters.

### 4. British Air Activity, Other Theaters.

a. North African Theater. 16 tons of HE were dropped on the harbor of Tripoli by 9 Wellingtons during the night of August 31-September 1. 2 motor vessels were reported sunk. Benghazi harbor was also attacked this night. 3 Heinkels began this attack by bombing a tanker and gasoline storage barge from an altitude of

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20 feet (?). At the same time the town was bombed by 2 Maryland bombers. 6 Wellingtons resumed the attack 2 hours later, dropping 5 tons of bombs. During the day of September 1, direct hits on the power station at Tripoli were claimed in an attack by 7 Wellingtons. Axis shipping and the munitions factory at Crete (?) were attacked on this day with good results by 7 Blenheims.

5. Axis Air Activity, Other Theaters.

a. Middle Eastern Theater. The Germans have based a squadron equipped with 6 Focke Wulfs at the Eleusis airdrome in Crete, apparently intended for operations against shipping in the Red Sea, according to a statement by the British Air Ministry.

LEK

I. B. # 8 , 3:00P, 9/3/41

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