4/16/38

c
o
p
y

Professor Irving Fisher
460 Prospect Street
New Haven, Connecticut

April 15th, 1938

Col. Marvin H. McIntyre
Secretary to the President
White House
Washington, D. C.

My dear Colonel McIntyre:

I would appreciate it if you could bring the enclosed letter to the personal attention of the President.

With kind personal regards.

Very sincerely,

(s) Irving Fisher

IF:M

Enc.

c

o

p

y

Professor Irving Fisher
460 Prospect Street
New Haven, Connecticut

April 15th, 1938

President Franklin D. Roosevelt
The White House
Washington, D. C.

My dear President Roosevelt:

After hearing you last night I wired you:

"Congratulations on magnificent message and fireside talk with the many constructive measures and proposals big enough to meet the big emergency. Probably you have now turned the tides of recession and distress as well as reassured those fearing more class warfare and failure of democracy."

This morning I received your kind acknowledgement of my letter of March 30th.

I also read the enclosed Times editorial which you doubtless have already seen. It has, for me, a twofold significance:

(1) Even the intelligent generally miss the main point of recovery--spending, namely the generation thereby of new bank deposits subject to check--"check-book money";

(2) The Times is however, in part right as to the long run. Your monetary measures have been mostly emergency measures and not yet permanent solutions of the money problem.

As to the present emergency, I urge that you give careful attention to the suggestion of Mr. Hemphill which he recently sent you, namely that you ask Eccles and the others concerned to "coin" or "monetize" the "float". This amounts to several billion dollars now always outstanding and unused of checks in process of collection. If these were made available for immediate credit to those who have deposited them, so that they would not have to wait nearly a week before this huge sum could be used, the result would be equivalent to the addition of (say) five billion dollars of circulating medium.

This measure, which requires no legislation, would, I believe make the proposed reduction in bank reserves unnecessary and would be far preferable because:

(1) The addition of the "float" to our circulating medium would come overnight as soon as the banks acted on telegraphed directions, while any considerable additional circulating medium through lowered bank reserves will require months of time.

(2) The "float" addition would be positive and certain while the other might never materialize at all, to any worthwhile extent.

(3) The reduction of the reserve requirements is a step backward toward the very instability which has been the fundamental trouble. I do not wonder that Chairman Eccles should be loathe to have to take this step.

But if it is to be avoided and the "float" monetization substituted, I imagine the initiative should come from you in view of the attitude of Secretary Morgenthau.

The "float" monetization would have the virtue, as compared with any other form of reflation, of causing no public alarm. You could then and, I believe, should reduce the scale of the spending program, which does cause alarm.

As to permanent monetary reform, it seems to me that legislation like that in the Binderup bill should soon be pushed, including the provision that all monetary action must be concentrated in the Federal Reserve Board, or some one responsible body and that none of it whatever should be in the hands of the Treasury.

If democracy is to be made to work and the executive departments are to be made efficient there must be no divided responsibility as to monetary policy. Moreover, the Treasury should not have any power to create the money which it spends. This is no reflection on Secretary Morgenthau but only on the present system.

If this system had not stalled and aborted reflationary effort, this recession could have been nipped in the bud.

Sincerely,

Irving Fisher

IF:M

THE WHITE HOUSE
WASHINGTON

April 16, 1938

MEMORANDUM FOR CHAIRMAN ECCLES

TO PREPARE REPLY.

F. D. R.

Enclosure

Form F. R. 131

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Mr Thomas
Mr Robinson (?)

Office Correspondence

Date April 19, 1938

To Dr. Goldenweiser

Subject:

From Mr. Clayton

The Chairman would like a reply prepared for the President to the letter of Irving Fisher. Mr. Fisher's chief burden is the Hemphill plan for monetizing the float on checks deposited in banks and I recall seeing the Hemphill plan which was the subject of his letter to the President of April 7, a copy of which was sent to Governor Szymczak and others of the Board, and is attached hereto.

The Chairman thinks the reply should refer to a memorandum prepared by the Federal Reserve which the President can enclose. In a discussion with the Chairman respecting the Hemphill plan, he thinks the following points, among others, could be made:

1. It would seem to require legislation to force all member banks to give immediate credit for deposited checks. Assuming that such drastic and ill-considered legislation were contemplated, it would be necessary to guarantee the banks against loss since banks would lose the protection which they now have of being advised by wire whenever items in any substantial amount (usually $500 or more) are unpaid upon presentation.

2. The banks already make available to responsible depositors the proceeds of deferred items, the resulting "deferment overdraft" being shown on control sheets which are usually checked each day by some officer of the bank.

3. While the suggested plan would make a large increase in the figure of demand deposits, would this necessarily mean that there would be any additional spending power? Except for the initial bulge, bank depositors would have the same monthly income so that it is not apparent that a stimulus to business would result.

On page 3 Professor Fisher suggests that permenent monetary reform should be pushed, including the lodging of all monetary action in the Federal Reserve Board or some one responsible body and that none of it should be in the hands of the Treasury. I presume the President would wish to duck this suggestion although he recently told the press that bank examinations should be in one Federal agency.

LC

April 29, 1938

My dear Mr. President:

In reply to your note of April 16 there is herewith submitted a proposed reply to Professor Fisher's letter to you. The reply answers the Fisher proposal by referring to the inclosed memorandum which deals with the Hemphill plan.

This plan is designed to increase spending by requiring banks to give immediate credit for checks in process of collection. It is my opinion that such a plan would result in little or no increase in the volume of spending and that there are serious legal and administrative objections to it. It seems doubtful to me that depositors would be induced by such a concession to increase their expenditures, which in the final analysis are determined by their incomes. The plan places undue emphasis on the effect of increasing the amount of deposits, whereas the more important elements in the business situation are those which determine how and at what rate available deposits are utilized. These latter elements are largely nonmonetary.

Respectully yours,

(Signed) M. S. Eccles

M. S. Eccles
Chairman

The President
The White House
Washington, D. C.

RIR:LC-mlg

LE R.I.R.
M.T.

Dear Professor Fisher:

This is to acknowledge your telegram of April 14 and your letter of the following day. I wish to thank you for your expression of approval of my message and also for your suggestions as to further possible measures for stimulating business recovery.

At my request Chairman Eccles of the Board of Governors has had prepared a memorandum on the Hemphill plan mentioned in your letter, and I am inclosing a copy of this memorandum.

Very truly yours,

FILE COPY

HEMPHILL PLAN FOR "MONETIZING" BANK FLOAT

A plan has been proposed by Mr. Robert Hemphill to increase the velocity of deposit circulation by requiring banks to give immediately available credit to the depositors of cash collection items. On some occasions banks defer the deposit credit in order to assure themselves that deposited items are "good" and collectible and also so as not to pay out funds before the collection proceeds are received. When a bank customer deposits a check drawn on a bank in another city the bank receiving the deposit does not collect the proceeds of the check until several days later, the time depending on the distance to the bank on which the check is drawn, the speed of communication, and the method of collection. Banks receiving checks on deposit in such circumstances usually reserve the right to withhold withdrawals from the deposit created until the collection of the deposited checks is completed.

If legislation were adopted to give effect to this plan it would be necessary to guarantee banks against losses which might result from granting immediate credit, since one of the common reasons now present for the deferment of credit is for protection against loss. In addition, it is not clear that legislation could be drafted which would forestall evasion of the essential provisions of this plan.

In addition to the legal and administrative objections to the plan, it seems clear that it would result in little or no increase in spending, which is its aim. The plan places undue emphasis on the effect of increasing the amount of deposits, the more important elements in the business situation are those which determine how and at what rate available deposits are utilized. These elements are largely nonmonetary. The expectation that spending would increase by a significant and permanent amount through the operation of this plan appears to be based on the incorrect assumptions (1) that there is a substantial amount of deposit credit deferred on account of collection, and (2) that this deferment acts as a continuously repressive influence on the velocity of circulation.

The amount of effectively deferred credit probably is not large. The cash collection items held by all commercial banks average about $2,500,-000,000 in most periods and seldom exceed $3,000,000,000, of which about three-fifths represents clearing house exchanges. Since these exchanges on local clearing houses are generally collected within 24 hours, the maximum amount of deposits subject to deferment is generally not much more than a billion dollars. The amount of deferment of deposit credit within this billion dollars is not large and, in view of the fact that demand deposits of individuals, corporations and partnerships in commercial banks total about $23,000,000,000, of which only about $2,000,000,000 are drawn on each day, the amount of delayed spending as a result of deferred credits probably is very small. It is doubtful that depositors would be induced by such a concession to increase their expenditures, which in the final analysis are determined by their incomes.

A review of commercial banking practices indicates that the effective deferment of deposit credit is not common, for the following reasons:

(a) Individual and business depositors whose accounts do not involve many large outside cash collection items ordinarily have all of the practical benefits of immediate credit on collection items. Banks allow immediate credit except in those circumstances in which the credit standing of the customer is not satisfactory, or in which the amount involved is large and the time of collection long so that the allowance of immediate credit would be the equivalent to an extention of credit. There is, of course, the usual reservation on the part of banks permitting them to withhold charges against an uncollected credit balance. This reservation usually takes the form of a statement on the deposit ticket and in the pass book of the following character:

> "The depositor agrees with the bank that credit allowed for items on this or any other bank or party is only provisional and until the proceeds thereof, in money, are actually received by this bank or items found good at the close of business of the day on which they are deposited; such items may be charged back to the depositor's account regardless of whether or not the item itself can be returned; that said bank may decline payment of any check drawn on such deposits until the items of this deposit, though credited, are actually paid in money."

(b) Commercial customers of banks depositing a large number or a large dollar volume of cash collection items, such as mail order houses, magazine publishers, and direct mail vendors, are usually allowed immediate credit for deposited items, provided that their credit standing is satisfactory. The banks receive compensation for this service in either of two ways, (1) by a direct charge for the collection of each item deposited, (2) or by requiring a compensatory balance, or what is sometimes called a "collected" balance. A compensatory or "collected" balance requirement is essentially the same thing as a deferment of deposit credit, but it results from a voluntary agreement between banks and their customers.

(c) Financial houses, commodity brokers and dealers, commission merchants, and others depositing large items requiring some time for collection and not offering satisfactory compensatory balances usually are not subject to the deferment of credit but compensate banks for the credit extension implicit in the process of collection by the payment of interest on the debit deposit balance (overdraft) or on the amount that the collected balance is overdrawn. This arrangement is similar in principle and in operation to English practice of making credit available by permitting overdrafts. It is commonly but not universally expected that collateral will be given for the total overdraft or for the overdraft of the collected balance.

It would appear, therefore, that the commercial bank restrictions on the use of uncollected funds are general in the sense that drawing against an uncollected balance on any one occasion is permissible but that day-by-day the banks expect customers to hold collected balances or to pay interest or other charges if uncollected balances are regularly drawn upon. In other words, the restrictions are imposed by account analysis rather than by specific deposit credit deferment.

The second assumption inherent in this plan is that deferment of deposit credit is a continuously repressive influence on the velocity of deposits, i.e., on their use. In view of the fact that the amount of deferment is small relative to the total volume of deposits subject to check and the free balances available are large relative to the amount of checks drawn upon them at any given time, it is clear that there are relatively few occasions when the use of bank deposits is restricted by credit deferment on account of collection items. In the final analysis the amount of payments made by an individual or business concern is determined by the amount of income, and abandonment of deposit credit deferment would have an appreciable effect on expenditures in the long run only if it permitted the carrying of smaller balances than would otherwise be carried. In any event the effect would not be more than an initial and temporary bulge: it would not have a continuous effect in increasing the use of bank deposits.