

BOARD OF GOVERNORS  
OF THE  
FEDERAL RESERVE SYSTEM**Office Correspondence**Date January 11, 1940To Chairman Eccles

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

From W. R. Gardner *WRG*

With reference to your contemplated meeting on the Inter-American bank proposal I am submitting three short documents. One of these gives a few notes on the status of the proposal so far as various participants in the discussions are concerned. The other two deal with the major questions that you have indicated you wish to raise: 1) Do we want a bank? 2) If we want a bank, what United States agency should participate in its capital and management? Both memos deal with the two questions and cover the same ground; but one memo covers the ground in 3-1/2 pages, the other in 2-1/2. The longer memo gives a more adequate explanation of its points; the shorter may be more convenient to glance at as a reminder in the midst of discussion.

January 11, 1940

THE INTER-AMERICAN BANK PROPOSAL

A. Do we want a bank?

1. Political considerations: The world situation is shifting rapidly under the impact of war developments. Organization of an effective group of neutrals in this hemisphere is difficult because Latin American countries have so many economic and cultural ties with Europe and their internal situations are far from stable. The establishment of institutions that will bring these countries together with the United States in the solution of common economic problems will, therefore, be constructive from the standpoint of our broader political problem. An Inter-American bank would appear to serve this purpose; but only if one can be devised which gives promise of conducting a reasonably safe business, for if the bank gets into serious difficulties it will become a political liability rather than an asset.

2. Economic considerations: To do an adequate business the bank would probably have to make long-term loans (regularly amortized) as well as short-term. It should have central bank or government endorsement of all its assets. Its assets should be guaranteed by the governments concerned against exchange blockage. Probably its business should be conducted in United States dollars only. It should be free to accept deposits from any source and to issue its own debentures.

Such a bank would be free of exchange risks, so far as the law can make it free; within each country it would have the strongest security possible; and its field of operations would probably be adequate to enable it to pay its way.

a. Possible constructive operations of the bank

- 1) Provision of better clearing facilities for exchange transactions among Latin American countries (probably not much scope for this).
- 2) Making short-term loans to meet seasonal and other temporary pressures on the exchanges (the Federal Reserve banks have made loans on gold for this purpose, but beyond this limited type of loan they have not gone).

- 3) Drawing to itself, by reason of its preferred international status, Latin American deposits that otherwise would be made in New York to escape domestic currency uncertainties; and reinvesting the funds in the country from which they were drawn (Latin American balances in New York have grown from about \$100,000,000 in 1933 to over \$300,000,000 today; in 1929 they were about \$200,000,000).
- 4) Making long-term loans which the private investment market is unwilling to make because of currency uncertainties, but which the bank could make because of its guarantee against exchange blockage. (The Export-Import Bank is making loans of this type today; but an Inter-American bank loan would throw less onus on the United States if eventually the debtor government has difficulty in paying.)
- 5) Sale of its own debentures in Latin American countries to supply outlets other than land or foreign securities for Latin American investment funds — these funds to be reinvested largely in the countries that supply them.
- 6) The bank's operations would force it to appraise the financial status and programs of various countries and offer it opportunities to make suggestions. Advice from the bank or insistence on sound financial practices would represent the collective judgment of a group of American countries and not just the self-interest of a single creditor -- the United States. It would tend to soften the charge of financial imperialism.

b. Limitations on effectiveness of the bank

- 1) Because of the great geographical distances and the paucity of able financiers in many of the countries involved, there will be major difficulties in organizing and administering an effective, yet representative, bank.

- 2) Most Latin American governments that are borrowing abroad are now in default. Several are subject to overthrow by revolution. It is a question what their promises would be worth either on securities or on a guarantee against exchange blockage. While they might be willing to give preferred treatment to the bank in practice, as well as in law, there is a possibility of the bank being seriously embarrassed by repudiations of promises.
- 3) Unless the bank's investments of United States funds in Latin American countries helped them to develop their export business and acquire more dollars, it would find itself getting paid only at the expense of other United States creditors of these countries. With currencies of the belligerents blocked it will be difficult for Latin American countries to acquire dollars unless they can increase their sales of goods to the United States. Will the bank program go hand in hand with an effective trade program? The recent breakdown of the trade agreement negotiations with Argentina is discouraging from this standpoint.
- 4) The possibility of destructive competition with Latin American branches of United States banks would require attention. This possibility, however, should be minimized if the Inter-American bank operates only in dollars.

B. If we want a bank, what United States agency should participate in its capital and management?

Presumably either the Treasury or the Federal Reserve System.

a. The argument for the Treasury is as follows:

1. The bank has a political significance. The Treasury is the financial arm of the administration.
2. Ultimately the greater part of the bank's business will probably be in intermediate or long-term loans similar to those made by the Export-Import Bank, R. F. C., and other Treasury banking organizations.

b. For the Federal Reserve System the argument is:

1. The Federal Reserve is (or should be) the representative of the Government in the field of bank operations. It is equipped to do a banking business -- even in the field of longer term credits for capital purposes.
2. Latin American countries have emphasized their conception of the bank as a central bankers' institution, calling attention to the shifting political personnel of their Treasuries and their lack of a well-developed banking knowledge and philosophy.

January 11, 1940

THE INTER-AMERICAN BANK PROPOSAL

A. Do we want a bank?

Political: Our Latin American policy would be helped by an Inter-American bank if it can do a safe and constructive job, however minor.

Economic: A potentially safe bank with an adequate volume of moderately useful business might be conceived as follows: Authority to make long-term as well as short-term loans. Central bank or government endorsement on all its paper. Assets guaranteed by governments concerned against exchange blockage. Power to accept deposits from any source and to issue debentures.

a. Constructive operations of bank

1. Better clearing facilities for exchange transactions among Latin American countries (probably not much scope for this).
2. Short-term loans to stabilize exchanges against temporary pressures (Federal Reserve bank gold loans do a little of this job now).
3. Return of Latin American dollar balances to their home countries.
4. Long-term loans which private investors are unwilling to make because of currency uncertainties (Export-Import Bank does this type of business now; but an Inter-American bank loan would throw less onus on the United States if payment difficulties arise).
5. Sale of its own debentures in Latin American countries to supply outlets other than land or foreign securities for Latin American investment funds -- these funds to be reinvested largely in the countries that supply them.
6. Financial advice to Latin American countries from a group of peers rather than from the United States which is suspected of financial imperialism.

b. Limitations on effectiveness of bank

1. Difficulty of creating an effective administration because of geographic separation and paucity of able financiers in Latin American countries.
2. Promises of governments on which the bank must depend may be no good. Most Latin American governments in default on their dollar indebtedness. A number of existing governments may be overthrown by revolution.
3. Latin American export trade to United States must be increased by the bank's investments of United States funds in Latin America; otherwise bank will find itself getting paid only at expense of existing creditors of Latin American countries. Will bank program go hand in hand with effective trade program? Breakdown of trade agreement negotiations with Argentina looks bad.
4. Possible destructive competition with Latin American branches of United States banks (would probably not occur if bank operates only in dollars).

B. If we want a bank, what United States agency should participate in its capital and management?

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STATUS OF THE PROPOSAL

1. The committee considering the Inter-American bank proposal is a sub-committee of the Inter-American Financial and Economic Advisory Committee, composed of representatives of 21 American Republics, which has been meeting in Washington now for two months. The sub-committee (which is one of three) is assigned the field of "Problems of Monetary and Financial Relationships". Its chairman is Mr. Sumner Welles, whose place has been taken in practice by Mr. Adolph Berle. The other representatives on the sub-committee are from Argentina, Bolivia, Colombia, Ecuador, Mexico, and Peru.

2. Mr. Berle has asked experts of the Federal Reserve and the Treasury to help him. The three outside economic advisers of the Treasury have been skeptical of the idea of a bank and have not participated in the more recent meetings on the question. Messrs. White and Bernstein have pushed the idea of a Treasury bank and have enlisted the Secretary's interest for such a proposal. The Secretary has written Mr. Berle expressing his interest in an Inter-American institution owned by governments and dealing with governments. The White-Bernstein group have worked out possible statutes for such a bank so far as ownership and management is concerned and have prepared a general list of objectives and functions. A copy of this plan was approved January 9 by the Secretary and will probably be sent to Mr. Berle today. Mr. Cotton, assistant to the Secretary in Latin American matters, is much more inclined toward central bank sponsorship -- particularly as regards Latin American countries.

3. The Treasury at its last meeting of Government experts on the bank question brought in Mr. Lincoln of the registration department of the S. E. C. He took little part in the meeting.

4. Until recently Mr. Berle has been depending almost wholly on Federal Reserve and Treasury experts. Recently, however, he has brought Mr. Collado of the Latin American section of the State Department into the picture and Collado is now playing a very active rôle. He was formerly with the Federal Reserve and continues to work closely with us.

5. The Latin Americans have indicated their attitude on a number of points, but are awaiting an American proposal. Mr. Berle hopes to be able to lay a tentative, but concrete plan of the bank before the sub-committee at its next meeting. It is expected that a meeting will be held at the end of the week. If so, any position we wish to take on the Treasury plan will have to be taken promptly.