Form F. R. 131

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date December 1, 1936

To Chairman Eccles

From Mr. Gardner WRG

Subject:

Here is the brief statement you requested yesterday with regard to recent Stabilization Fund operations. I attach a clipping I have just received from this morning's Herald Tribune that shows the press has already caught on to what's happening. Henceforth the Treasury will have no secrecy unless it changes its methods.

RECENT STABILIZATION FUND OPERATIONS

1. The picture with regard to Stabilization Fund operations appears to be as follows, although in the absence of direct Treasury information, it is partly guesswork:

For three weeks the Stabilization Fund's account at the New York Federal Reserve Bank has been down to a bare working minimum. That is, its dollar resources are practically exhausted. It is not in position to buy any more gold. When the British Fund wishes to exchange gold for dollars in order to support the pound, our Fund must sell an equivalent amount of domestic gold to the Federal Reserve Bank of New York in order to acquire dollars with which to buy the British gold. On November 9 it sold $21,000,000 of gold to the bank. Last week it appears to have sold about $28,000,000 more in three installments.

2. Since gold sold by the Fund to the Federal Reserve bank gets into reported monetary gold stock, this stock rises without corresponding imports, for the gold obtained from the British Fund is earmarked abroad. The press has been slow to raise any questions about this; but the questions are now beginning, and it will not be long before the conclusion is drawn that these unexplained increases in monetary gold stock represent Stabilization Fund operations. At this point the Treasury may want to restore the secrecy it formerly enjoyed.

3. There are certain steps the Treasury might take to obtain secrecy that would be undesirable from the standpoint of the Federal Reserve System. One would be the purchase of $500,000,000 or $1,000,000,000 of Treasury bills with Stabilization Fund gold, so that the Fund could thereafter sell Treasury

bills to the market whenever it had to acquire dollars for additional purchases of gold. Such a move, while it would enable the Fund thereafter to operate in secrecy, would immediately add $500,000,000 or $1,000,000,000 to member bank reserves and leave the Fund with a great open-market portfolio that could be used for any purpose the Treasury saw fit. Such a move would, therefore, not only intensify the excess reserve problem but might seriously interfere with the work of the Open Market Committee.

A far more constructive type of Treasury bill operation would be for the Treasury to borrow initially from the market in order to buy gold. A question may, however, be raised whether the Treasury could justify increasing the public debt for the purpose of buying an unproductive asset -- such as gold.

A procedure that would provide the Fund with ample dollar resources and prevent subsequent gold purchases from affecting monetary gold stock would be for the Fund to sell say $500,000,000 of gold certificates to the Federal Reserve Bank of New York, taking the proceeds in an account with the bank, either directly or through various channels that would serve to conceal the nature of the operation. Gold movements would then have their usual effect of increasing or decreasing member bank reserves, but the Fund would engage in no open-market operations. This procedure would appear to be satisfactory from the standpoint of the Federal Reserve System.

4. It would be useful to know if the Fund has already been dealing in Treasury bills. There is some reason to believe that it has.

It would also be useful to know if the Fund has any way of obtaining additional resources other than that of converting its gold into dollars. Can the Treasury appropriate or lend cash to it for use in stabilizing the dollar, or can the Fund itself borrow from the public? There is some evidence that transactions of this character have already occurred. If such sources can be freely tapped without further Congressional authorization, then there is a real possibility of handling a gold inflow so as not to affect member bank reserves.