Currency Sug
not used

See Treasury file for final memo

December 10, 1936.

TREASURY PROPOSAL FOR STERILIZING GOLD

The substance of the Treasury's proposal is that it will offset the effects on member bank reserves of any further additions to the gold supply, either through import or through domestic production. It is proposed to offset them by selling bills to the market.

This proposal would have the great merit of rendering our reserve position independent of gold movements. While, however, we recognize that it would be an effective means of coping with the problem of further additions to the excess reserves of member banks, we feel that there is some question whether it might not be desirable to postpone the contemplated action until certain other matters that will arise in the next few months are first disposed of. These matters are possible action that may be taken by the Board with reference to reserve requirements and possible legislation relating to capital inflows.

With reference to excess reserves, the question of the desirability of raising reserve requirements will undoubtedly shortly arise. The support for such a step would be seriously weakened and the whole question be complicated if the Treasury adopted the proposed policy at this time. It might be said that there was nothing in the current situation that warranted <u>two</u> drastic steps within such a short space of time. Moreover, it might strengthen the case of those who feel that the tax payer rather than the banks should bear the costs incident to the handling of the excess reserve problem. The Treasury's interests, of course, lie in the opposite direction and it would, therefore, appear to be to its advantage to postpone action until it ascertains what steps, if any, the Board proposes to take with reference to raising reserve requirements.

Similar considerations arise in connection with possible legislation to discourage capital inflows. The interests of the Treasury in representing the tax payers, and the interests of the Board, in preventing further growth of deposits and reserves, both lie in the direction of devising a really effective check to further capital inflows. Public discovery of a hitherto unknown way of sterilizing gold would greatly strengthen the case of those who will oppose any legislation designed to deter foreign investment here. Furthermore, it might conceivably be interpreted as the solution to the problem we have been asked to study, as minimizing the danger of new tax legislation and hence be followed by an accelerated rate of inflow of foreign capital.

In view of the fact that the quantitative effect of sterilizing the relatively small inflow of gold in the next two months would not be commensurate with the probable adverse psychological effects it would appear the wiser course to defer action at this time.