November 8, 1937.

GOLD STERILIZATION POLICY

The proposal has been made that the Treasury announce immediately that it is prepared to desterilize up to approximately $1,000,000,000 of gold, held in the inactive account.

This proposal would have immediate beneficial effect provided funds so derived were applied to purchasing power through relief or other channels and not used to retire debt. The effect of desterilizing would be to add an equivalent amount at once to bank deposits, with a corresponding increase in excess reserves. This would provide the Treasury with funds without borrowing and thus increasing the public debt and without new taxes. Existing appropriations can first be drawn upon to meet such increased relief, agricultural and other requirements as may be necessary this winter and as further funds are needed they can be obtained as required by desterilizing. This purpose could be announced at once and would give assurance that the debt is not to be increased to meet added relief needs, and that new taxes are not going to be imposed. It can be made clear that this backlog will be drawn upon only as needed pending business revival that will absorb the load on the Government.

At the same time gold outflow can be met out of the stabilization fund; dollars so derived from release of gold can be used to buy bills, i.e., reduce debt. This is the only way in which the stabilization fund can be readily used for this purpose. If gold inflow is resumed, the process can be reversed, as an automatic mechanism.

Merely to desterilize and reduce debt would be to lose the stimulus that urgently needs to be given to purchasing power, particularly at this moment. It would reduce debt at the outset but an increase of the debt would result later, and such a sequence of events would injure the Treasury's position and prestige. The effect from a monetary standpoint of desterilizing and paying off debt would be to pile up another billion of idle funds on top of the billion already existing. That might tend to unstabilize interest rates by pressing them down to unsustainable levels, but otherwise it would be without influence. It would not relieve the Treasury of the prospect of more borrowing as revenues fall off and relief needs increase.

This proposal might cause a seriously adverse psychological reaction, however, unless it is emphasized that Congress will be asked to make provision to absorb resultant excess reserves when it becomes necessary to do so in order to prevent a credit inflation.