

December 20, 1937

DISCONTINUANCE OF STERILIZATION BY
THE TREASURY

Following are reasons why an announcement by the Treasury at this time that it is going to discontinue its policy of sterilizing additions to the gold stock would be undesirable:

1. There is no object in doing it now from the point of view of member bank reserves, because in recent months gold has been flowing out of this country. Since October 6 the United States has lost about \$140,000,000 of gold. At the present time there is little movement in either direction since continued reductions in foreign balances are being approximately offset by a heavy surplus of merchandise exports.

It is impossible at this time to predict whether gold movements in the next few months will be inward or outward. It is likely, however, that no large movements in either direction will occur.

2. If what is desired is to create a psychology of fear of inflation, then discontinuance of sterilization would be a minor and ineffective measure, because it would be generally understood that this is only a gesture, since there are no gold imports to sterilize.

3. For the same reason discontinuance of sterilization is not likely to have any effect on domestic commodity prices.

4. Definite and final discontinuance of sterilization by the Treasury would constitute an abandonment of control by this country of the effects of gold imports on the domestic situation. Henceforth the monetary conditions in this country and the reserve position of member banks would be

determined in large part by economic conditions and policies abroad rather than in the United States.

5. Once abandonment of the policy is announced it will be difficult to resume the practice.

6. Consequently, if the Treasury ceases to desterilize, the whole problem of future gold imports, which in the long run are likely to be large, will rest on the Federal Reserve authorities which will not have adequate means of coping with the situation. They have exhausted their power over reserve requirements and their power of absorbing excess reserves in the future is limited.

7. The direction and volume of the gold flow depends to a considerable extent on the gold content of the dollar, on exchange stabilization, and on our policy in regard to taxation of foreign balances and profits. The Federal Reserve System has no authority over these policies and should, therefore, not have the sole responsibility for regulating the influence of gold movements on our economy,

8. It would be much better not to make any announcement at this time, to continue sterilization of such gold imports as may occur, and to leave the determination of the amount of gold to be desterilized and the best time to do it for the future. Such a policy would keep the control over the effects of gold in our own hands; it would make it possible, through desterilization and reesterilization, to add or subtract from member bank reserves amounts to be determined at the time - in accordance with current developments.