Form F. R. 131

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date October 30, 1939

To Chairman Eccles

Subject:

From Emile Despres

You may find the attached two items on gold of interest.

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Form F. R. 131

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date October 19, 1939

To Chairman Eccles

Subject: Note on Gold

From Emile Despres

On thinking over our discussion of Wednesday, I am strongly inclined to believe that it would be most unwise to suggest at this time any spectacular action with respect to gold, such as a cessation of gold purchases. In the first place, unless we had a fully developed spending program to take its place and were confident of being able to put the program through, cessation of gold purchases would have a substantial depressing effect on our internal economy. Our export surplus averaged about $100,000,000 a month during 1938 and about $55,000,000 a month during the first eight months of this year.

In the second place, it seems to me unlikely that the President would give serious consideration at this time to any proposed measure which would substantially impair the ability of Great Britain and France to obtain American goods.

In the third place, cessation of gold purchases would amount to a virtual admission by the Administration that we are stuck with the gold we have, and the internal political effects of such an admission make action of this sort impracticable on these grounds.

Your objective of eventually achieving a rational gold policy would best be served, in my judgment, by merely proposing at this time that we quietly and informally ask the British and French Governments that, so far as possible, they finance their purchases of goods from us through the sale in the United States of income producing assets, and that they try to keep their sales of gold to us within reasonable limits. First, such a step would not interfere with British and French purchases in this country and, in fact, would help to assure Britain and French access to American supplies. There is a widespread popular feeling in this country that we are getting stuck when we exchange our goods for useless gold, and the public's attitude towards British and French purchases here would be far more favorable if these purchases were being financed through the sale to us of income producing assets. The prevalence of this sentiment is revealed in the many wisecracks about digging gold out of a hole in South Africa and burying it in a hole in Kentucky. To the average person, selling our goods in exchange for gold seems only slightly less foolish than selling on long term credit. (If you wish to use this point, it seems to me highly important to make it clear that you are merely describing the temper of popular opinion. The effectiveness of your argument would be greatly weakened if the impression were given that you were expressing your own opposition to our supplying economic aid to Great Britain and France.)

Second, our chances of not getting stuck with the gold we already have will be somewhat improved if we ask Great Britain and France to sell us their earning assets first and to regard their gold holdings as a last reserve. If these countries, which together hold nearly half of the monetary gold outside the United States, dispose of the bulk of their holdings during the course of a prolonged war, the prospects of a return to some form of international gold standard will be slight. After the close of the war, their need for American goods in connection with their own reconstruction will be much more urgent than their need for gold, and there can be little doubt that they will develop a monetary system which obviates the use of gold. If, on the other hand, these countries retain a portion of their gold reserves, their interest in restoring gold as a basis for currency and crddit and as an instrument for settling international balances will be somewhat greater.

Third, the substitution of securities for gold would help to minimize the further expansion of our already redundant credit base.

The attached table summarizes our estimates of foreign holdings of gold, dollar balances, and American investments at the outbreak of war. For France, Great Britain and the British Empire, these three items amounted to about $10,000,000,000; the British Empire's gold production was $750,000,000 in 1938, and can probably be stepped up by about 15 per cent within two years. The table does not include privately hoarded gold, nor does it include the large volume of earning assets apart from American investments which could be disposed of in this country to obtain needed supplies of dollar exchange. Our trade with all foreign countries produced an export surplus of $11,000,000,000 during the last war. Under present conditions, commodity prices are likely to rise less sharply in response to wartime demands than during the last war. Moreover, Great Britain and France, during the present war, will obtain a much larger proportion of their foodstuffs and raw materials from Empire sources and a considerable portion of the export proceeds accruing to the Dominions will be used to retire their outstanding long term debts to Great Britain.

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FOREIGN HOLDINGS OF GOLD, DOLLAR BALANCES, AND AMERICAN INVESTMENTS -- END OF AUGUST 1939

(In millions of dollars)

Type of holding	World (Outside U.S.)	Un.Kgdm. France & Br.Emp.	Germany Italy & U.S.S.R.	Smaller Eur. Countries	Non-European Neutrals
Gold reserves	11,740	5,740	1,370	3,600	1,030
Dollar balances	2,910	1,270	30	870	740
Securities readily negotiable (Est. market value)	2,820	1,420	1/	2/980	420
Gold, dollar balances and securities	17,470	8,430	1,400	5,450	2,190
Investments not readily negotiable (Various bases of value)	2,440	1,570	1/	2/670	200
Total gold and U.S. Assets	19,910	10,000	1,400	6,120	2,390
Annual Gold Production 1938	1,150	750	1/180	20	200

1/ Small amounts, not shown separately in available sources; included in figure for smaller European countries.

2/ Includes German, Italian, and Russian holdings; see note 1/.

Mr. Despres
Mr. Morse

From the office of
JOHN G. TOWNSEND, JR.
Washington, D. C.

October 26, 1939.
FOR IMMEDIATE RELEASE.

SEEKS CHANGE IN GOLD POLICY

Although the gold standard is now virtually extinct, the United States is still steadily adding to its vast hoard of the yellow metal, Senator John G. Townsend, Jr. of Delaware today advised the Senate. Although $4,000,000,000 was enough gold to finance the dangerous speculative boom of 1929, devaluation of the dollar produced a stock of $7,438,000,000 in 1934.

Yet in less than six years since then, our stock of gold has increased to more than $17,000,000,000, said the Delaware Senator, who last Spring introduced a resolution calling for an investigation of the gold policy.

While no action was taken on the Senator's resolution, a similar resolution was later introduced by Senator Wagner and passed by the Senate. The investigation for which it provided, however, has not yet been begun.

The following is the text of Senator Townsend's statement today on gold:-

> The problem of gold must be faced by the American people sooner or later. The longer the delay, the more costly the solution will be.
>
> In 1933 the Treasury and Federal Reserve banks held $4,200,000,000 of gold. After the price of gold was increased by almost 70 percent (from $20.67 a ounce to $35) our centralized gold stock was valued at $7,438,000,000. In the less than six years since then it has grown to more than $17,000,000,000.
>
> Even in these days of billions, this stock is of fantastic proportions. It is considerably more gold than is held by all the other governments and central banks and stabilization funds of the entire world. It is equal to three-fifths of the world's gold stock. Our proportion of the world's gold, moreover, is increasing weekly. Merely during the 12 months through September approximately $3,300,000,000 of the metal was acquired by this country.
>
> Much of this huge gold stock lies idle, a dead asset in Kentucky. It is owned by the nation, but it is not used by the people. It earns no interest. It is not at work. The Federal Reserve System has $5,500,000,000 of excess reserves.

The Treasury holds approximately $2,000,000,000 of gold sterilized. (1) Indeed, if so much gold were not held sterile and idle, this country might even now be feeling its inflationary effects. Only $4,000,000,000 of gold was sufficient to support the inflationary boom of 1929. It is easy to imagine how much inflation our present $17,000,000,000 of the metal could support.

It is practically certain that this country can never dispose of its surplus gold for what that metal has been costing. Since we raised the price to $35 an ounce, gold has come here from all parts of the globe. Every gold miner has been on our dole, from South Africa to Siberia. Current news reports that Russia is sending 17½ tons of gold here for the purchase of American goods is typical of what has been going on for years.

The gold we have imported has been paid for dearly. It has been bought with the products of our industry and our agriculture. In 1932, before revaluation of the dollar, it took less than 24 bushels of apples to buy an ounce of imported gold. Today it takes 50 bushels.

In 1932 it took about 40 bushels of wheat to buy an ounce of imported gold. Today, despite the 80 percent increase in the price of wheat, it still takes over 38 bushels to buy an ounce of gold.

In 1932 it took 313 pounds of cotton to buy an ounce of gold. Today despite the large increase in the price of cotton, it takes 380 pounds of cotton to buy the same amount of gold.

There would be no objection to paying such increased amounts of our real wealth for foreign gold if we needed the metal in our monetary system. But today there is absolutely no need for more gold. Las January the Board of Governors of the Federal Reserve System reported to Congress that since 1933 reservebalances of member banks has increased threefold, due principally to the gold inflow. The Board pointed out its helplessness to counteract (2) "an injurious credit expansion".

Even though we do not need or use the imported gold, its purchase might be excusable if only we knew that we could at will dispose of it again for what it has cost us. The American people will not wish to use this gold to buy foreign apples, wheat,cotton or motor cars. Such imports would affect our industry and agriculture adversely.

Even if there were not this obstacle, it is obvious that the $9,383,000,000 of gold we have acquired abroad since 1934 could not be spend abroad for these or other commodities in an equal period of time or even in a much longer time without causing a rapid in-

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(1) $1,800,000,000 or more in the Stabilization Fund and $194,000,000 in the General Fund.

(2) Twenty-fifth Annual Report, pp 22-3.

crease in the prices foreigners would demand for their goods.

It is significient that the gold standard is today virtually extinct. Only one country, Belgium, maintains its currency freely interchangeable with gold, at a fixed price.

What this country should do with its present surplus of billions of dollars of gold is a question that need not and indeed cannot be determined now. But it has long been clear that the nation needs no more foreign gold. Withouth changing the monetary value or price of gold at home, it would be a perfectly simple matter to cease buying the imported metal. Such a step today would involve no deflation. We would still have $17,000,000,000 of gold. We should still have $5,500,000,000 of excess reserves. The main change effected would be that we would not be increasing our gold stock and our excess reserves by importing more gold.