BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
Division of Research and Statistics

BUSINESS AND CREDIT CONDITIONS

CONFIDENTIAL

June 4, 1937
Cr. 13

C O N T E N T S

Cr. 13
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BUSINESS AND CREDIT CONDITIONS

Outlook

Economic conditions register "fair and cooler." The tone of business is more sober and sounder than it was six months ago. There is not so much forward buying, but no interruption in the volume of output. Private construction, particularly for business purposes, continues to expand. The Board's index of industrial production will be 119 for the second quarter of the year and for the third and fourth quarters is not likely to fall below 115, which was the level for the last quarter of 1936.

While there is still a considerable volume of unemployment, chiefly among common laborers, shortages of skilled labor have developed in some lines and wage advances have been numerous. The rise in labor and other costs may be a retarding factor for further expansion of activity, but the strong demand for goods caused by accumulated shortages and the increase in buying power providesa strong foundation for a sustained level of output.

Agricultural production is likely to be in good volume this year and the income of agriculture, as well as of industry and labor, is at a considerably higher level than in 1936.

Prices of raw materials, which had advanced sharply in the latter part of 1936 and early this year, have declined and are now in better alignment with prices of finished products.

Bond prices, both United States and corporate, have had a considerable downward readjustment from their high levels of last December, and stock prices have shown substantial declines after an almost continuous rise lasting for two years. Capital issues, particularly for refunding, have been in reduced volume and the outlook in the capital market is somewhat uncertain.

Government security holdings of the banks in large cities have been substantially reduced, particularly during March, but this liquidation appears to have run its course. There is evidence of continued shifts from long to short maturities. Demand for commercial loans continues to increase. Bank deposits have been reduced, chiefly through withdrawals of funds by the United States Treasury and through reductions in interbank balances.

Short-term rates for money have firmed slightly and long-term rates have advanced. Rates for both kinds of money, however, are still at extremely low levels, owing chiefly to the large supply of investment funds.

After completion of the readjustment to increased reserve requirements, member banks still have approximately $900,000,000 of excess reserves, of which about $200,000,000 is held by the banks in the New York money market.

The flow of gold to this country continues unabated and the amount held by the Treasury in the inactive account accumulated since the closing days of 1936 is in excess of $800,000,000. In recent months, however, foreigners have not been purchasers of American securities on balance, as they had been previously, and the inflow of gold has corresponded to a growth in foreign balances held by American banks.

Business Prospects

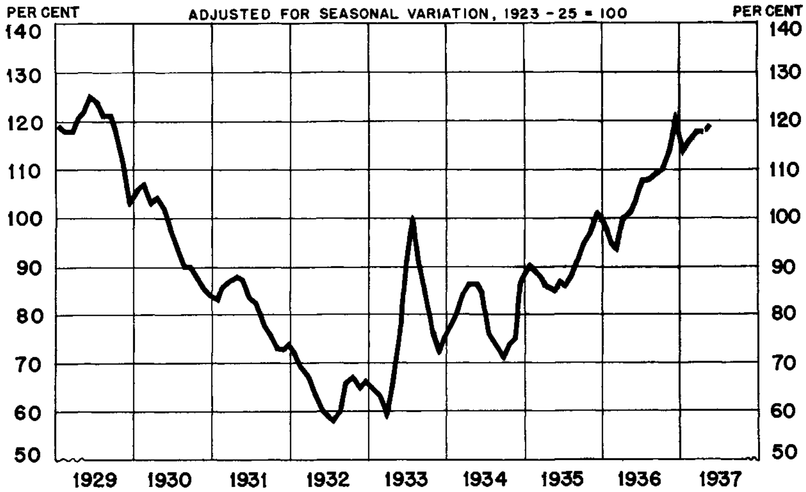
The course of economic activity and income has been sharply upward for two years and a half. There has been little interruption in this advance, partly because continued expansion in many lines has provided increased income and buying power which has resulted in quickly arresting such declines in activity as have occurred in other lines. By last autumn stocks of many basic agricultural and industrial commodities had been considerably reduced and demand for commodities became strong both in this country and abroad and for armament as well as for industrial purposes. There was some delay in filling orders, speculative buying increased, prices of raw materials and semifinished products rose sharply, wage rates advanced, and the rise in prices extended to many finished products. Continuation of these developments threatened to lead to serious maladjustments and a sharp decline in activity.

During the past two months, however, there have been declines in prices of many of those raw materials and semifinished products that earlier had risen most, and buying of these commodities has been less active. Prices of finished goods have advanced somewhat further and prices of raw materials and finished goods are now in somewhat better alignment than at the peak of the rise. For commodities in general the decline, as indicated by the Bureau of Labor Statistics index, has been only 1 point following upon an advance of 7 points.

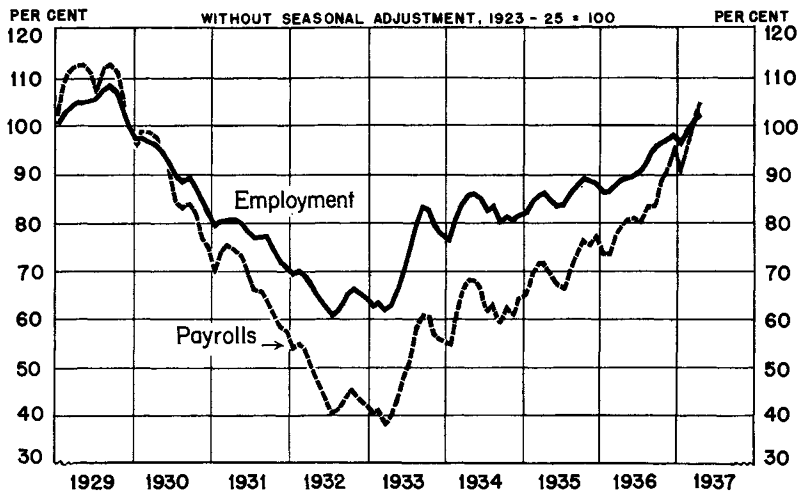
In most lines the reduction in buying from earlier high levels has not resulted in a slowing up in production, partly because a large volume of unfilled orders had accumulated. Retail prices are advancing and this will tend to limit somewhat the expansion in the physical volume of trade accompanying increasing incomes in both urban and rural areas. The underlying demand situation, however, is so strong that the outlook is for continued growth in activity and incomes or for maintenance at present levels. If there is any decline this year, it will probably be small in amount, limited to a few industries, and last for a short time. Agricultural output will probably be larger this year than last year, with a sharp increase in crops and little change in output of livestock products. In the construction industry, which has lagged behind many others in the recovery, the prospect is for further growth. While public construction has declined this year, private construction is continuing to expand, particularly in the industrial, commercial, and utility fields. The rise in building costs, amounting to 10 to 15 percent, appears to have retarded the advance in residential building somewhat but, with increases in building costs in the near future probably limited to wage advances, with rents and values continuing to advance, and with mortgage rates declining, residential building is likely to expand later in the year by a considerable amount.

The course of industrial production, factory employment and payrolls, and wholesale commodity prices is shown on the accompanying chart.

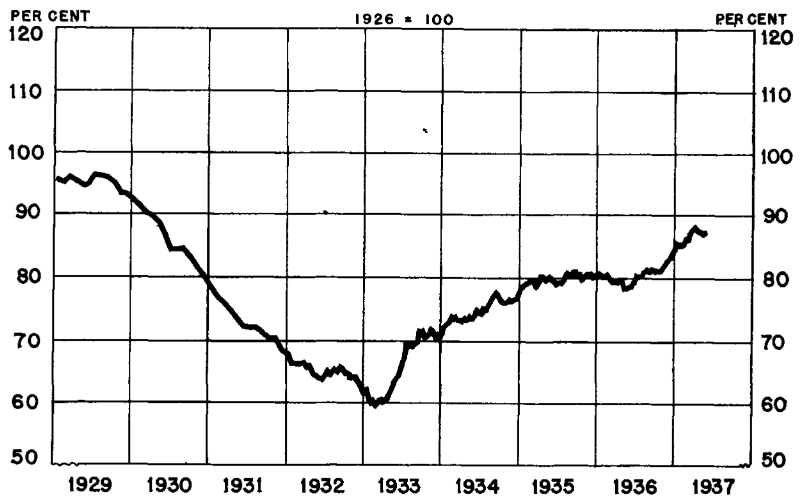
INDUSTRIAL PRODUCTION



FACTORY EMPLOYMENT AND PAYROLLS



WHOLESALE PRICES



Banking and Credit

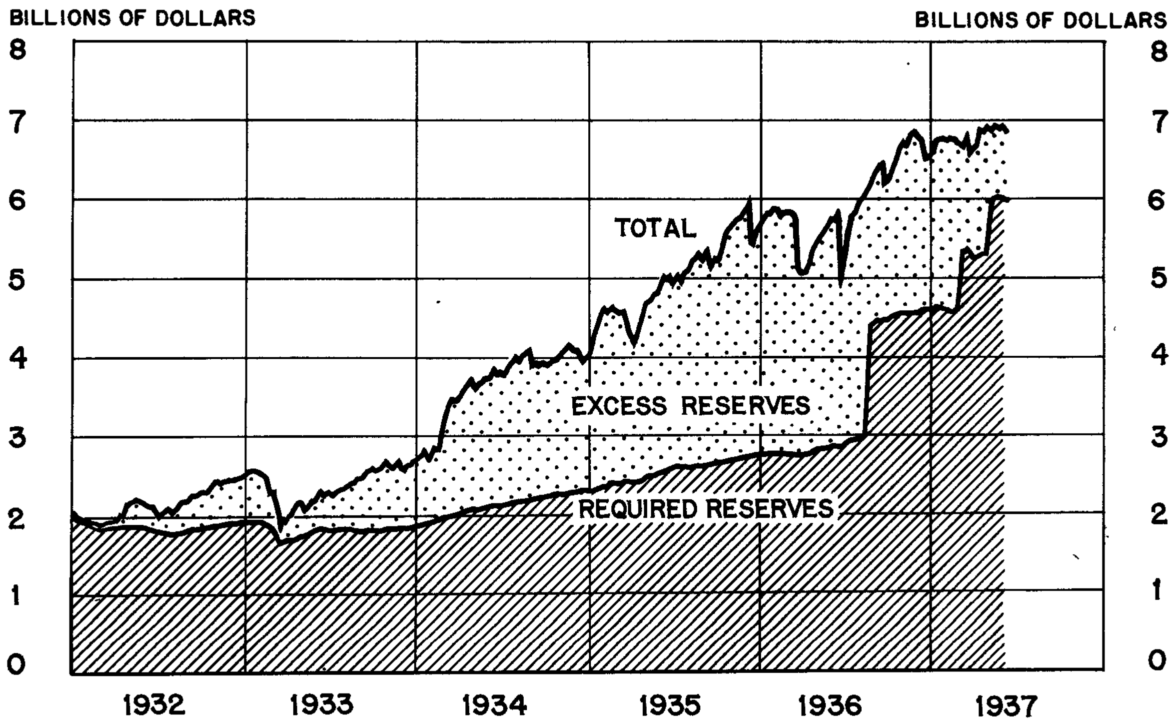
Excess reserves

Adjustments by member banks to the higher reserve requirements appear by now to have been largely completed, leaving all classes of banks with substantial excess reserves. Borrowings by banks showed little increase around May 1 and have since declined. At reporting member banks in leading cities withdrawals of bankers' balances by country correspondents continued during May, but city banks gained funds from other sources and maintained adequate reserves without reducing their loans and investments. Excess reserves held by the various classes of member banks as of the last week in May are given in the following table. The chart shows changes in total reserves and required reserves during recent years.

RESERVE POSITION OF MEMBER BANKS
Daily average for week ending May 28, 1937, partly estimated
(Amounts in millions of dollars)

	Reserve balances	Required reserves	Excess reserves	
			Amount	Percent of required reserves
Central reserve city banks				
New York City	2,726	2,482	244	10
Chicago	591	545	46	8
Reserve city banks	2,251	1,954	297	15
Country banks	1,382	1,029	353	34
All member banks	6,950	6,010	940	16

MEMBER BANK RESERVE BALANCES



In the following week excess reserves were reduced to $860,000,000, principally as the result of an increase of $90,000,000 in money in circulation, which reflected in part holiday demands and in part the effect of a strike of armored-car employees in New York. New York City banks showed a decline of $110,000,000 in excess reserves, while there were increases elsewhere.

During the next few months member banks as a whole will probably continue to hold a substantial volume of excess reserves. Treasury fiscal operations around the middle of June are not likely to cause substantial changes in excess reserves, unless there be a large volume of cash subscriptions for the new Treasury securities. This is unlikely in view of the reduced volume of idle funds held by banks. Interest payments and redemption of maturing bills by the Treasury should provide the market with sufficient funds to offset payments on income taxes and on cash subscriptions to the new issue. There may be some further withdrawals of balances by banks in the interior and some increase in required reserves, but there is no reason to expect the development of a tight situation.

Excess reserves may decline to below $700,000,000 around July 4, when there is large demand for currency, but for most of the summer they will be considerably above that figure. So long as the Treasury continues its present policy of neutralizing the effect on reserves of increases in the gold stock, the principal factors affecting the volume of excess reserves will be changes in required reserves and money in circulation. Deposits may be expected to increase somewhat or to maintain the increase expected around June 15. The existing volume and distribution of excess reserves provides the basis for an expansion of bank loans and investments.

The growing demand for loans is likely to continue, and the liquidation of Government securities by banks appears to have been completed, although there may be a gradual decrease following additional purchases in June.

While money in circulation will probably average somewhat higher during the summer months than during May, no important absorption of reserves from this source is expected to occur until next fall. At the July 4 peak, money in circulation will probably be about $125,000,000 above the May 26 level or $40,000,000 above that of June 2. Practically all of this additional currency may be expected to return during the month of July, but from then until Christmas the trend of money in circulation will be upward. During August money in circulation may be from $50,000,000 to $100,000,000 above the May level, and at Labor Day it may be about $200,000,000 higher.

It appears unlikely that any important changes will occur in the other items affecting excess reserves over the summer months. The Treasury has been maintaining a balance of around $100,000,000 with the Reserve banks and any substantial change from this level will probably be of short duration. There is no way of anticipating possible changes in reserves that would result from disbursements by the Treasury of its free gold and silver holdings which aggregate about $200,000,000 at the present time.

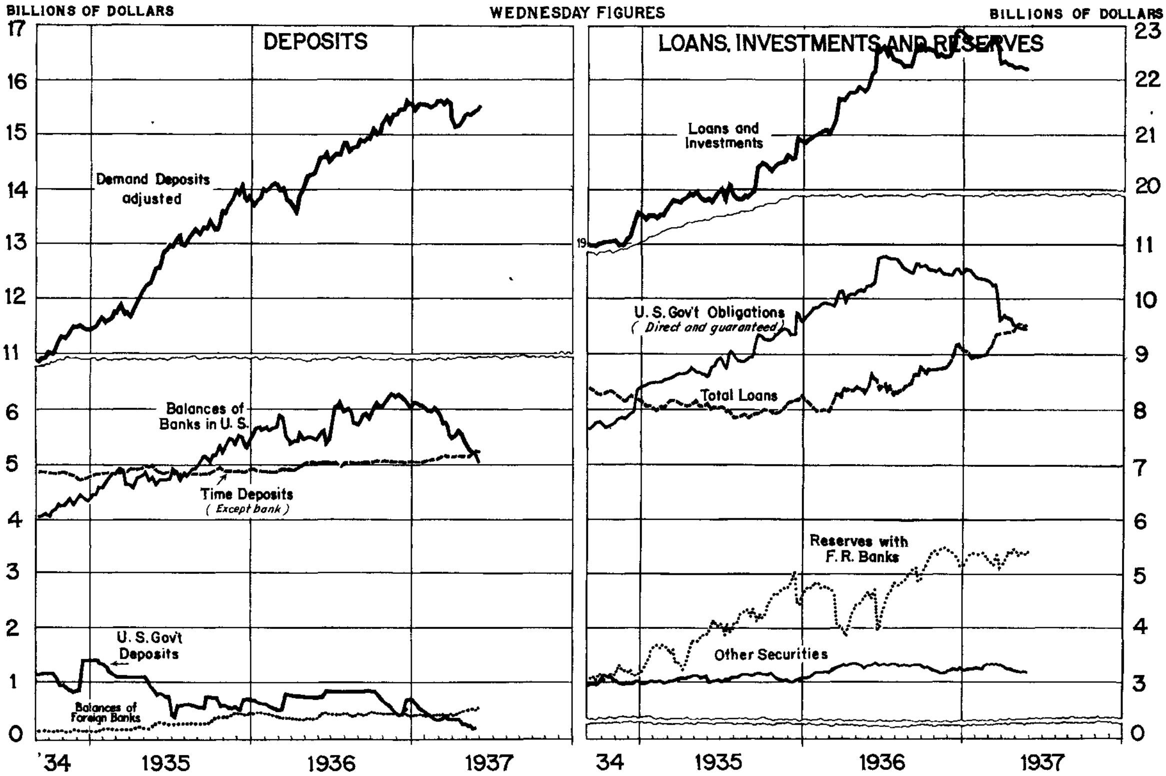
Recent changes in bank deposits

Since the beginning of 1937 there has been some decline in the total amount of member bank deposits, accompanied by important shifts in the distribution of deposits. These changes in deposits had the result of reducing required reserves by more than $100,000,000 below what they would otherwise have been. The declines, as shown in the chart, occurred principally in deposits of the United States Government and in interbank balances.

Interbank deposits increased considerably from 1933 through 1936, with the large growth in excess reserves held by banks, and at member banks in leading cities balances of domestic banks amounted to more than $6,000,000,000 at the end of 1936, as compared with an average of about $3,000,000,000 held for many years prior to 1933. By May 26, 1937, they had been reduced to about $5,000,000,000. Much of the previous accumulation of bankers' balances represented the redeposit by banks with their city correspondents of funds received on deposit from other banks. Reporting member banks in leading cities reported a decline of $550,000,000 in their balances with other banks between the end of December and May 26. It would appear that in this period nonreporting banks withdrew on balance about $450,000,000 of their deposits from city correspondents.

These withdrawals of bankers' balances reflected principally adjustments by member banks to the increased reserve requirements. Country banks in recent years have carried a portion of their idle funds in excess reserves with Federal Reserve banks and a portion on balance with correspondents. Banks having insufficient excess reserves with the Reserve banks to meet the increases in requirements drew upon their balances with other banks. Also in the spring banks in agricultural sections customarily draw upon their balances to meet payments in urban areas for seed, machinery, and other supplies and equipment required by farmers in that season. Some banks probably in addition used balances to meet withdrawals of United States Government deposits in this period.

REPORTING MEMBER BANKS IN 101 LEADING CITIES



In addition to large withdrawals of bankers' balances there has been a substantial reduction in United States Government deposits at member banks since the first of the year. On June 1 Treasury balances in special depositaries amounted to $140,000,000 as compared with $990,-000,000 at the end of 1936.

Time deposits at reporting banks have increased somewhat this year, mostly in New York City, and balances of foreign banks have also increased, reflecting the recent inflow of short-term capital from abroad.

Adjusted demand deposits, which were sharply reduced in March, owing chiefly to Federal tax payments and to the sale of Government securities by banks, have subsequently increased. On May 26 they were about where they were at the beginning of the year, both at New York banks and at banks outside New York. Increases in adjusted demand deposits since March, during a period when total loans and investments of reporting banks have shown little change, are attributable chiefly to Treasury expenditures from accumulated balances. Since these balances have been reduced to unusually low levels bank deposits cannot continue to be built up from this source, but deposits are likely to increase as the result of a further growth in bank loans and of purchases by banks of new Government securities issued to provide funds for gold purchases.

Cessation of heavy selling of Government securities

Holdings of United States Government obligations at reporting member banks, which declined sharply in March and moderately in April, showed little further change in May. It appears, however, that banks have been purchasing additional Treasury bills and selling longer-term obligations.

Sales of Government securities by banks began in New York City in the summer of 1936 and in other leading cities this February, and were heaviest during March. From July 1, 1936, to May 5, 1937, United States direct and fully guaranteed obligations held by reporting banks declined $1,100,-000,000 in New York. From January 6 to April 28 they declined by $460,-000,000 at reporting banks outside New York. Holdings of Government securities at all classes of banks outside New York had increased during the latter half of 1936, and during the first quarter of this year holdings at country banks showed a slight increase in contrast to the large decline at city banks.

Further increase in commercial loans

Since January there has been a further growth in borrowing at reporting member banks for business purposes, as indicated by increases in so-called "other loans" through May 12 and in the newly reported item of commercial, industrial, and agricultural loans since that time. From the end of January through May 26 the growth in these loans amounted to about $450,000,000, which was almost twice as much as the increase during the corresponding period of 1936 when commercial borrowing was resumed on a substantial scale. Of the recent growth about $210,000,000 has occurred in New York City, $60,-000,000 in Chicago, and most of the remainder in the Eastern Federal Reserve districts, excluding New York City, and in the San Francisco district, although increases were general. Since the latter part of April the increase has slackened, reflecting in large part seasonal influences, but further increases may be expected from the middle of the summer through December.

Loans to brokers and dealers in securities have increased since last autumn. On May 26 such loans at reporting member banks amounted to

$1,320,000,000, which was about $175,000,000 larger than during last October. This increase has accompanied a somewhat larger growth in stock brokers' advances to customers on margin accounts. Loans on securities to customers and loans on real estate at reporting banks have not changed appreciably this year. Loans to other banks and borrowings of reporting member banks increased just prior to the raising of reserve requirements on May 1, but they were subsequently reduced.

Figures from the call report for March 31 show that at country banks there was a small growth in "other loans" of about $50,000,000 during the first quarter of 1937. Since March a year ago the increase in total loans of country banks has been substantial, amounting to about $300,000,000 or nearly 8 percent. Loans on securities declined by about $30,000,000, while loans on real estate increased by over $100,000,000, most of which was on urban property. Other loans to customers increased by nearly $150,000,000 and holdings of open-market paper by $70,000,000.

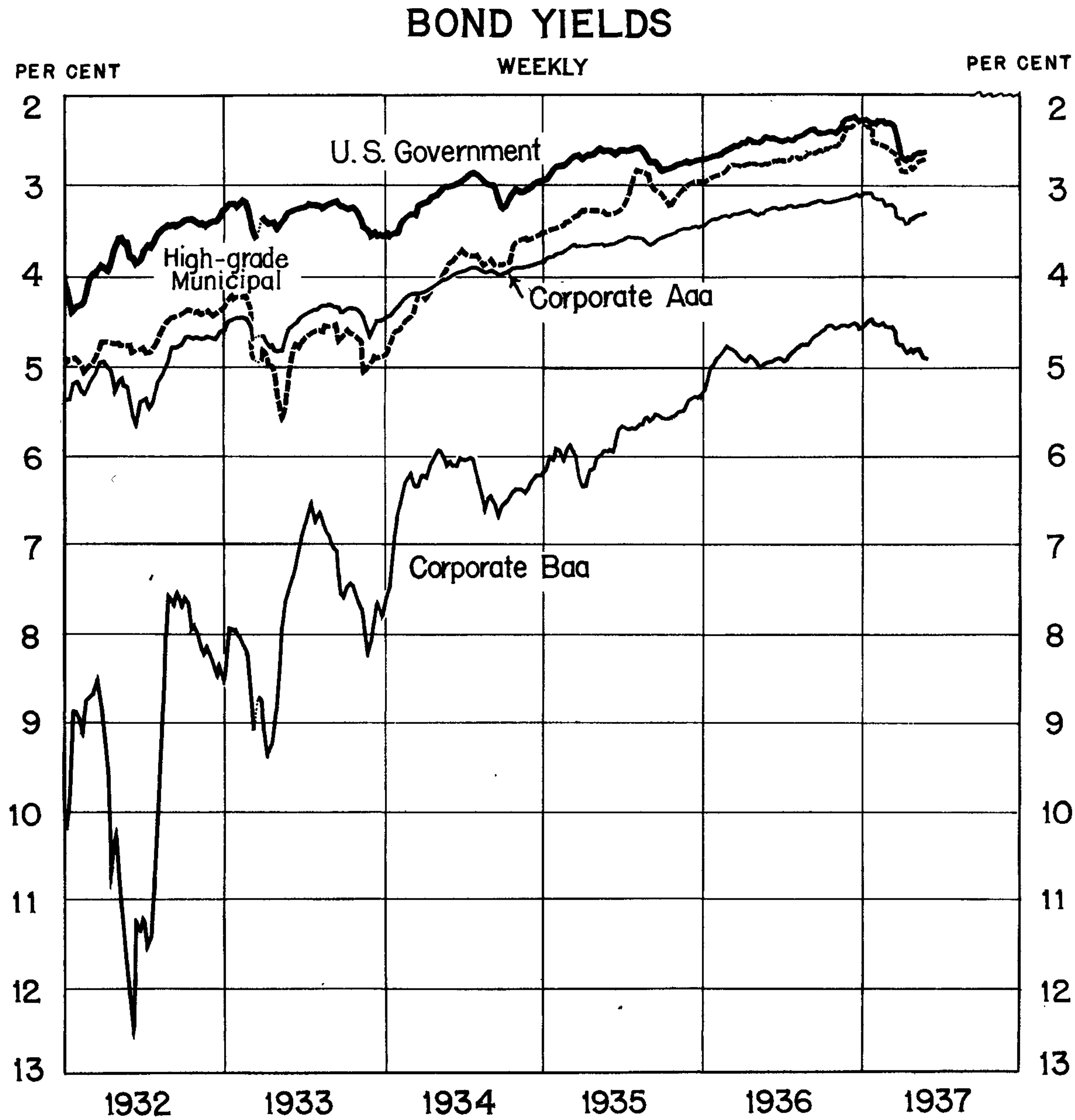
Security Markets

During the first four months of 1937 security prices showed larger declines than at any time since 1933 or 1934. These declines followed rapid advances in 1936 to new high levels for bonds and to the highest levels since 1930 for stocks. In December 1936 yields on short-term Government securities rose fairly rapidly and yields on long-term Treasury obligations rose slowly, reflecting declining prices. Prices of municipal bonds began to decline sharply in the early part of January and the decline in high-grade corporate bonds commenced a little later. Fluctuations in bond yields during recent years are shown in the chart.

In March prices of all types of Government securities declined rapidly. The yield on 9-month Treasury bills rose to over 0.70 percent during March, compared with a low of 0.08 percent in November. The average yield on 3-to 5-year Treasury notes increased from 0.92 percent early in December to 1.70 percent early in April, and the yield on Treasury bonds callable in more than eight years rose from 2.22 percent to 2.78 percent.

Since early April, however, the Government security market has shown a firm tendency. The principal strength has been in intermediate Treasury bonds, but the average yield on Treasury notes had declined to 1.47 percent on June 1, and the yield on long-term Treasury bonds to 2.63 percent.

The decline in prices of high-grade corporate bonds, which commenced in the middle of January and culminated in a final drop in the early part of April, was followed by an irregular upward movement in April and May.


BOND YIELDS
WEEKLY
PER CENT
PER CENT
2
3
4
5
6
7
8
9
10
11
12
13
U. S. Government
High-grade Municipal
Corporate Aaa
Corporate Baa
1932
1933
1934
1935
1936
1937

Moody's average of Aaa bond yields was 3.30 percent on June 1, compared with 3.48 percent at the high point in April and with 3.07 percent at the low in January. At present high-grade corporate bond yields are lower than at any time prior to March 1936.

Lower-grade corporate bond yields according to Moody's average of Baa bonds have also risen since the beginning of the year and have shown no net recovery since April. Yields on the Baa bonds, however, have remained lower than at any time prior to 1936.

Stock prices, after reaching a new low for the year on May 17, rose somewhat and at the end of May were about 13 percent below the peak on March 10. The Standard Statistics index of prices of 419 common stocks in the last week of May was at 117 percent of the 1926 level, or about the same as the first part of last October.

Factors in decline in bond prices. - The magnitude and suddenness of the decline in bond prices during the early months of this year were in many respects unprecedented and were to a large extent the result of a series of transitory developments. The underlying situation remains strong since there is a large supply of funds seeking investment with a relatively small demand for new capital by industry and a declining demand on the part of the Federal Government, the largest borrower in recent years. Recent confidential estimates of the volume of savings in the United States, made by the research staff of the Securities and Exchange Commission, indicate that savings in 1936 amounted to about $5,700,000,000, as compared with $2,100,000,000 in 1935, and a 1925-1929 average of less than $10,000,000,000. During 1936 savings in monetary form -- individuals' bank deposits, cash holdings, and investments in life insurance and building and loan associations -- were more than twice as large as the annual average for the 1925-1929 period, while the public's investment in securities was smaller than the sums received as amortization and redemption payments and from foreigners for the purchase of securities in this country. Moreover, the supply of inactive deposits at banks in financial centers has continued large. Insurance companies and other institutional investors still hold unusually large cash balances.

The increase in reserve requirements for member banks removed from the market a considerable amount of funds that offered a potential demand for bonds but were not active in the market, remaining in the form of idle balances. After the increase banks still have an abundance of idle funds. Sales of securities by banks that may have been necessitated by the increase in requirements did not reflect a general shortage of funds, but were the result of readjustments of reserve positions by individual banks, especially by city banks subjected to substantial withdrawals of bankers' balances. In many cases the adjustments made were larger than were in fact needed, and some banks with adequate reserves also decided to sell or at least refrained from buying before prices should decline further. For a variety of reasons many banks chose to sell long-term bonds rather than to dispose of short-term assets, notwithstanding the fact that yields were much larger on bonds than on short-term paper. Probably the principal factor in this situation was that banks had paper profits in their bond accounts and wished to realize them before they diminished or disappeared all together.

Other factors in the decline of bond prices were that the large volume of new corporate and municipal securities issued in December and January with exceptionally low coupon rates were not readily distributed, that rapid increases in commodity and stock prices indicated possibilities of inflationary developments, and that income tax collections fell below budget estimates.

Firmness in the market since early in April has reflected a diminution in sales by banks, especially since final readjustment to the new reserve requirements, continued purchases by other investors, and the purchases of $96,000,000 of Government securities by the Federal Reserve System.

Capital issues. - In December 1936 and January of this year an unusually large volume of new security issues was sold at low rates. After the middle of January, when the decline in bond prices began, offerings sold less quickly and a number of issues had to be repriced at lower levels before they were finally disposed of. Under these conditions, offerings of new securities were considerably curtailed in March, April, and May. This decline reflected principally a reduction in the volume of municipal issues from the unusually large amount sold in January and a decrease in the amount of corporate refunding issues. Issues to raise new capital declined somewhat in April and were further reduced in May.

CAPITAL ISSUES

(In millions of dollars)

	Total issues	Domestic Corporate			Municipal	Foreign
		Total	New	Refunding		
1936--Mo. av.	518	382	99	282	93	12
1936--December	726	626	218	408	97	0
1937--January	603	299	95	204	206	73
February	497	354	130	225	44	74
March	382	319	138	181	59	0
April	272	172	85	87	80	20
May (estimated)	200	115			41	0

Since the middle of April, when the downward movement of high-grade bond prices was halted, new security issues have generally been distributed without repricing, although sales have sometimes been slow. A few issues which were priced below the market sold at premiums, in contrast to the situation in February and March, when the pricing of an issue below the market frequently had the effect of pulling down the rest of the market.

Corporate issues offered for new capital purposes in the first quarter of 1937 were larger in amount than in any of the first three quarters of 1936. Statistics on these issues cover offerings to secure funds for repayment of bank loans and other unfunded debt, as well as for plant and equipment and for working capital purposes. Registration statements of securities sold in the first quarter of 1937 suggest that about half of the "new capital" uses were for increasing working capital, and about one fourth for the acquisition of plant, equipment, and real estate. These are about the same proportions as were reported for the fourth quarter of 1936.

A new feature in the financing of recent months has been the offering of a larger proportion of issues for both new and refunding purposes to security holders of the issuing corporation. In most of the months of 1936 the amounts so offered were less than 10 percent of the total amounts offered. In the first 4 months of 1937, however, issues offered to own security holders were about 22 percent of the total amount offered.

About 35 percent of the corporate financing for new capital purposes in the first 4 months of 1937 was by railroads. Petroleum companies and those classified as "other industrial and manufacturing" accounted for another 35 percent. Issues for new capital by public utility companies and by companies in the metal and mining industries have been relatively much smaller than during 1936.

Unless business has a serious setback there appears reason to expect a further increase in the amount of corporate securities offered for new capital purposes. Other sources of funds for these purposes, such as earnings of corporations, their accumulated cash, and bank loans, will be factors in the situation but will probably not supply a larger proportion of funds in the future. Substantial refunding issues, however, similar to those offered in 1935 and 1936, may not be offered again until major uncertainties concerning interest rates have been eliminated. Availability of investment funds for the purchase of securities may be affected by further borrowing by the Treasury to meet budget requirements and to pay for purchases of inactive gold. Banks, moreover, may not take so large a proportion of new Treasury offerings as in the past, thus leaving a larger volume of securities that will need to be absorbed by other investors.

Treasury Finance

Present indications of Federal receipts and expenditures for the current fiscal year ending June 30 indicate that the deficit, exclusive of statutory debt retirements, will be about $2,560,000,000, compared with deficits of from $3,000,000,000 to $4,400,000,000 during the fiscal years 1934 to 1936.

Indicated receipts and expenditures for this fiscal year are compared with actual figures for last year in the table below.

TREASURY RECEIPTS AND EXPENDITURES
(In millions of dollars)

	Indicated, fiscal year 1937	Actual, fiscal year 1936	Increase (+) Decrease (-)
Receipts	5,260	4,120	+1,140
Expenditures, excluding debt retirements:			
General: 1/			
Adjusted compensation payments	560	1,670	-1,110
All other 1/	4,560	4,030	+530
Recovery and relief	2,700	2,780	-80
Total expenditures	7,820	8,480	-660
Deficit	2,560	4,360	-1,800

1/ Includes all expenditures for emergency conservation work and in 1937 indicated expenditures of $400,000,000 for the social security program as compared with $28,000,000 in the fiscal year 1936.

The substantial decrease in the deficit as compared with last year results in part from a large increase in receipts and in part from the difference in adjusted compensation payments. Although actual receipts have been considerably less than anticipated in January the total for the year will probably be about $1,100,000,000 larger than during the preceding year and will be the highest of any fiscal year since 1921. The increase in receipts results from larger collections of income taxes, some miscellaneous internal revenue taxes, and customs duties, and also from the new social security taxes, which are now yielding substantial revenue.

Total expenditures, exclusive of statutory debt retirements, will be about $660,000,000 less than in the fiscal year 1935-1936. If adjusted compensation payments are excluded, however, the total will be about $400,-000,000 above the level of the three preceding years. General expenditures in 1937, exclusive of adjusted compensation payments, will be larger than in 1936, owing to expenditures for the social security program. Gross expenditures for recovery and relief will be slightly larger than last year, although net expenditures shown in the table are smaller, reflecting larger offsets in the form of repayments to Government credit agencies.

In recent months Treasury fiscal requirements have been increased through the Treasury policy of holding gold acquisitions as inactive monetary stock. Since the gold sterilization program was inaugurated in December the Treasury has purchased $800,000,000 of gold. A substantial portion of the requirements of the Treasury during the present fiscal year for budget purposes and for purchases of gold for the inactive account has been met by drawing on the Treasury working balance. The working balance reached its highest level of $2,400,000,000 in March 1936, when the Treasury was making preparations for the redemption of Adjusted Service bonds. At the end of 1936 the balance, exclusive of gold, amounted to about $1,200,000,000, and on June 1 was $260,-000,000.

Since the end of December the gross debt of the Treasury has increased by about $800,000,000. This increase, as shown in the following table, was principally in the form of United States Savings bonds and various special issues. Treasury bills increased by $350,000,000, but the increase in Treasury bonds reflected exchanges for maturing notes.

UNITED STATES GOVERNMENT DEBT
(In millions of dollars)

	December 31, 1936	May 29, 1937	Change
Treasury bonds 1/	19,531	20,015	+484
Treasury notes	10,289	9,764	-525
Treasury bills:			
Regular 9-month	1,953	1,953	0
Tax date	250	600	+350
U.S. Savings bonds	475	775	+300
Adjusted Service bonds	451	405	-46
Special issues	752	1,078	+326
Noninterest-bearing debt	707	622	-85
Total	34,407	35,213	+806

1/Including a small amount of pre-war open-market issues.

On June 15 the Treasury plans to sell approximately $800,000,000 of Treasury notes. In addition to receipts from the sale of notes, the Treasury in June will receive a net amount of about $200,000,000 in cash, representing principally income and other tax receipts in excess of budgetary expenditures.

There will be cash expenditures of $300,000,000 for the redemption of maturing Treasury bills and of about $200,000,000 for the purchase of inactive gold. As a result of all transactions during the month the Treasury's working balance will rise from the present level of about $300,-000,000 to approximately $1,000,000,000 at the end of June.

During the second half of the calendar year it is estimated that Treasury cash requirements for budget expenditures will be about $200,000,000. This deficit, however, is likely to be more than met by receipts for unemployment trust funds and the sale of savings bonds. If purchases of gold continue at their present level, however, it will be necessary for the Treasury to sell more open-market securities before the end of the calendar year.

Gold and Capital Movements

During the period of the new international currency arrangement (October 1936 - May 1937) the United States has acquired from foreigners about $1,150,000,000 of gold. At the outset this movement of gold reflected largely purchases by foreigners of American securities. In the six weeks following inauguration of the arrangement, foreigners' investments in American securities were extraordinarily heavy. As this movement receded to more ordinary levels, another type of security transaction assumed importance. Purchases of foreign securities in New York became heavy, chiefly in connection with Argentine conversion operations. In common with other raw material countries Argentina has been experiencing a rapid strengthening of its international position and was able to provide for redemption of its high-coupon dollar bonds in part by utilizing its existing dollar resources without the necessity of borrowing. A substantial part of the borrowing was done in England which bid actively for the Argentine refunding issues in this market.

The movement of foreign funds into foreign securities in New York continues, but since the middle of March, when the downturn in the American stock market began, foreigners have purchased less in American securities. In fact in April foreigners turned sellers to the extent of $40,000,000, and in May buying has been intermittent.

At the beginning of April a new factor entered the situation. A flow of short-term funds from Europe set in on a scale greater than the previous movement into securities. This appears to be associated largely with various aspects of the foreign attitude toward gold.

Early in April there were widely credited rumors of an impending reduction in the United States gold price. A combination of factors lent plausibility to the rumor that the gold price was about to be lowered. Reluctance to buy gold was apparently indicated by the British Fund and several developments in America clearly showed that the gold problem was being seriously considered here. Among such developments were the adoption of the sterilization policy last December; the subsequent discussion of proposals to curtail the unwelcome inflow of foreign capital and gold; and the President's statement on April 2 that certain commodity prices were too high.

The President's statement on April 9 that he knew of no plan to reduce the gold price appears to have reassured the markets. Speculation for a rise in the dollar gradually subsided, but the uncertainty created by the discussions regarding gold led to continued dishoarding on a large scale. The reluctance of the British Fund to buy this gold resulted in large sales to the United States -- a process which forced sterling up on the exchange market and stimulated a movement of short-term funds from London to New York on the part of those who believed the rise in sterling to be temporary.

At the end of April the British Fund entered the bullion market on a more substantial scale. Sterling was held steady at its new high level, which, however, the market still appears to have regarded as temporary. The United States continued to draw a considerable part of the gold available on the London bullion market although, in addition to British buying, there were large Dutch purchases. Since the middle of April the gold holdings of the Netherlands Bank have increased by $145,000,000, which probably represents approximately the amount of gold acquired by the Dutch Fund during that period. The movement of gold to the United States in May was increased by certain official sales for the purpose of accumulating dollar balances.

At the end of the month further gold rumors and new international complications in Spain brought an intensification of the dishoarding movement and a heavy transfer of funds to New York, in conjunction with which sterling declined from $4.94 to $4.92.

The inward movement of gold in the two months in which short-term balances have dominated the picture has been on as large a scale as during movement of foreign capital into American securities last fall. Both periods were characterized by extensive dishoarding of gold, but, whereas dishoarding in the fall appears to have been induced by the opportunities for investment, dishoarding this spring occurred at a time of stock market weakness and may indicate uneasiness as to the future of the gold price.