

• See also Strong's correspondence with
Case (on domestic problems)

Burgess

Jay

Harrison

Nason

Saylor

Gilbert

Stewart, W W

Smith, Colman

Kenzel

and Part II Aug - Sept. 1925

Part I - Contents noted
GHR
11/12/63

INTERVIEW WITH STANLEY BALDWINLONDON, TUESDAY, JULY 7, 1925.

He seemed very glad to see me; expressed a good deal of concern about Mrs. Morgan's illness and the effect it might have upon her health permanently, and upon Mr. Morgan.

After the usual complimentary exchanges, I asked him if he would mind telling me something about the labor and trade situation; that we had heard so much about bad trade in England, about the difficulties with labor, etc., that it was giving us some concern, and I had wondered at times whether there might be some exaggeration of the type which we find at times in a country like England, where they are always willing to face the worst of the situation and state it.

He said that in point of fact the trade situation was bad, and causing them considerable concern; that the difficulties with labor were spotty at the present time, the coal trade presenting the greatest difficulty. He said that they thought they would face a struggle with coal labor, but that this was a time when they could afford to do so, when the demand was slight and stocks of coal on hand enormous.

He expressed himself as hopeful of a successful outcome of the negotiations for the security pact, although again that would prove to be a very difficult negotiation indeed.

I asked him if he regretted the debt settlement, and he said that while the service of the obligation was always a matter of concern to them, and the difficulties would likely increase rather than decrease while British trade was so bad, he did not regret the settlement and that the advantages of the generally changed attitude in America toward Great Britain, of which that was largely the cause, more than offset the purely fiscal difficulties involved.

He was anxious to know how I felt about the prospect of settlement of the debt questions with the allied countries, as they describe France, Italy, and Belgium, to which I replied that I had left too soon really to be conversant

with what was taking place, but that I still feared that the French proposals especially would be of a character that would leave the negotiations somewhat up in the air, unless, indeed, the monetary and fiscal crisis in France was of a character which impelled them to make a real settlement and a real adjustment of their domestic difficulties.

He expressed the keenest appreciation of the result of the negotiations between Norman and myself looking to the resumption of specie payment; said that they had had quite a battle with some of the opposition to immediate resumption, but, on the whole, he thought it had gone with greater success than they had anticipated. He thought that the strong gold position of the Bank was a surprise. And he also said that he had occasion recently to make a statement in the House of Commons in which he had spoken very frankly his belief that this arrangement and other arrangements of similar character which were necessary in such affairs were possible because of relations of mutual confidence, which had peculiarly characterized the relations between himself, Governor Norman, Jack Morgan and myself.

He exacted the promise that I should have another visit with him when I go back.

CONVERSATION WITH MR. HOUGHTON

LONDON, JULY 7, 1925.

After leaving Mr. Baldwin, I went to the Embassy and found Fred Sterling there, but the Ambassador engaged. He said to wait and he would cancel some engagements. Meantime Bill Phillips, our Ambassador to Belgium, came in, whereupon Mr. Houghton cancelled all of his engagements and we spent the morning together until nearly one o'clock.

The first part of the talk had to do entirely with the negotiation of the proposed pact. Mr. Houghton had just seen Austin Chamberlain, the Foreign Minister, and went over all the ground with Phillips so that he would be conversant with it on his return to America. The substance of it, leaving out the great mass of detail, was that Germany had made a proposal to the French dealing with principles which should apply to middle European peace. These, as I recall them, were - (1) mutual compact for France and Germany not to attack each other, (2) Germany was to be left free to negotiate for the absorption of Austria, for the rectification of the eastern frontier, and for the rearrangement of the situation in Upper Silesia, where the big coal areas are; Germany obligating herself not to resort to war or military measures, but to diplomatic negotiations, possibly with the assent of the powers; (3) England would retain entire freedom of action, her obligation of guaranty being to take sides with either France or Germany in case willfully attacked by the other, and to use influence, without guaranty or other obligation, to maintain peace on the eastern frontier.

This proposal by Germany England believed could be put into workable shape, but the French had dispatched a reply to Germany which was highly legalistic and contained conditions which Germany would find it impossible to accept, one being absolute obligation by Germany to respect the present frontier lines on the

east, and reserving the right of sanction, which I gathered principally meant the right to send troops through Germany for the defense of Poland in case of war with Germany. Germany would join in the guarantee of present western frontiers.

Mr. Houghton felt that Germany was in danger of making the serious mistake of meeting the French on their own ground of highly technical, legalistic discussion in their reply, raising all sorts of objections, which would have the effect of giving Germany the appearance before the world of raising obstacles to the pact which contains the germs of real peace in middle Europe.

A large part of the discussion had little bearing upon our affairs, and need not be included here. At the end, however, Mr. Houghton said that he wanted to talk with me further. I had to leave to keep an appointment at the Bank, but undertook to meet him at his house at 5:00 o'clock, which I did. He then outlined a plan which he was reducing to writing for a general agreement among the nations which would open the door to a very extensive military disarmament, - to include the United States, England, France, Belgium, Germany, Italy and Japan. He was working it up for the President, believing that the only hope for some universal plan of disarmament would be some scheme of this sort, undertaken under the auspices of the President and at his initiative.

He then gave me a long description of conditions in Germany, and something of personalities. As to the latter, he said that Hindenburg had proved to be a level-headed, sensible president, with a very high sense of honor. When difficulty arose in getting candidates and the nationalists approached Hindenburg he at first declined summarily. On second approach, which was made with great urgency, he replied that he had given a personal oath of allegiance to the Kaiser, and under those conditions it was impossible for him to become a candidate and take the oath of allegiance to the republic. He was then persuaded that he was mistaken in his position and went personally to the Kaiser to be released from his oath, which the Kaiser granted him. And when he was elected he took the oath to the

constitution; and Mr. Houghton said thereby he gained the confidence of the great mass of people who otherwise would have had no confidence in him whatever.

He spoke very highly of Dr. Luther, Chancellor, but regarded the rest of the cabinet as men of small caliber, some of them, in fact, being bureau chiefs who had been given cabinet positions because of the difficulty of getting men of the usual type.

He said that Dr. Schacht had gained a great position for himself; that he was very able and resourceful and was earnestly devoting himself to real work of reconstruction and to carrying out the Dawes Plan; that he had great influence with the Government; was very vain; and had a predilection for making political speeches, some of which were very indiscreet; that his friends had remonstrated with him, not always with success. He thought it was an excellent thing for me to meet him, and that it would help him by strengthening his influence.

Mr. Gilbert, he said, made a great impression in Germany; his report, as well as his actions, were regarded as strictly neutral, unprejudiced, and fair. So much so, indeed, that President Hindenburg had sent for him recently and told him this personally, and thanked him.

He spoke very highly of the work that Shepard Morgan is doing.

Also he said that Dr. Schacht was very much under the influence of Governor Norman, which spoke well for the outlook for the Reichsbank.

Then, when it came to a discussion of the political situation, he went over the points mentioned at the morning meeting and asked me if I would find opportunity, if it came in conveniently, to tell Dr. Schacht that in his opinion it was most important that the German reply to the French note should avoid raising all sorts of objections which would enable the French to say "There are the Germans again rejecting the opportunity for a peaceful adjustment of affairs; they are always to blame." I told Mr. Houghton that this was somewhat outside of our line, but I might have opportunity to drop a hint to Dr. Schacht on my own responsibility, or possibly as coming directly from Mr.

Houghton

I gathered from what Mr. Houghton said as to conditions in Germany, that he was definitely impressed with the fact that political tranquility was now possible in a domestic sense; that Germany would suffer to a considerable extent as the result of the loss of the discipline that was imposed upon all of the men of the nation by army service; that that was the kind of training they were accustomed to and needed, and that on all hands he had heard regrets expressed, even by the people of the lower class, that they no longer had the advantage of the kind of training and discipline which the army afforded. He felt that the period of self denial, economy, heavy taxation, etc., which they were now facing, with inadequate supplies of capital, and with this change in the preparatory training of young men, would give them a period of rather bad times, but that the industrial establishments were in apple pie order, with immense facilities for production, and when they emerged from the readjustments now impending they would be a severe and probably successful competitor for the world's trade.

He thought that the reports indicated an excellent crop outlook for this year, with less need for buying food abroad. But that was almost the only particularly favorable development of the moment.

This conversation bears so directly upon the discussion at luncheon at the Reichsbank today (July 11, 1925) that I will skip directly to our meeting at luncheon, when Governor Norman and I joined Dr. Schacht, the Chancellor, Dr. Luther, and the Minister of Foreign Affairs, Mr. Stresseman.

Berlin

FEDERAL RESERVE BANK OF NEW YORK 7.11.25.....

CONVERSATIONS WITH DR. SCHACHT

BERLIN, JULY 10- , 1925

Reichsbank Position:

The new bank law requires the Reichsbank to maintain a reserve against its note issue of 40%, of which 30% must be gold, and 10% may be divisen.

The position of the Bank, the economic situation in Germany, and, ultimately, the success with which transfers may be effected under the Dawes Plan depend, in a monetary sense, entirely upon developments in the note issue, the reserves, and especially the divisen of the Reichsbank.

The status today is as follows:

Gold Held at the Bank ----- M. 975,000,000

to which add

Gold Received from Norway
as the result of settlement of
the Herring Account ----- 22,500,000

Gold just Purchased from the
National Bank of Switzerland ----- 30,000,000

Gold actually Held Abroad ----- 90,500,000

TOTAL GOLD RESERVE ----- M. 1,118,000,000

The Divisen Account stands as follows:

Balances Held Abroad in Banks
Subject to Immediate Withdrawal ----- M. 360,000,000
(This is the amount shown in the
Reichsbank Statement)

Allowing for certain changes which were taking place at the time the figures were given us, the reserve position as of a few days previous showed roughly M. 1,460,000,000 gold and divisen against nearly M. 2,500,000,000 notes, or about 58%.

In addition to the divisen shown in the statement, the Reichsbank holds bills and investments abroad which are not subject to immediate call, but may be gradually made available, amounting to M. 302,000,000. This appears in sundry of their accounts, and is the reserve out of which demands for foreign

Reichsbank Position (cont'd)

payments are now being met by Germany, which are gradually reducing available supplies of divisen at the rate of from M. 7,000,000 to M. 10,000,000 a week. The loss, however, has been much more rapid than this during the past few months, being no less than M. 420,000,000 between April 15 and July 12.

An inspection of the large reduction of M. 420,000,000 makes it appear that this is not as serious as the figures would indicate. Out of the divisen which he had on hand early in the year, he was obliged to pay 5,000,000 sterling to the Bank of England in repayment of their loan; something like 45,000,000 marks in settlement of the herring account in Norway; about 22,500,000 marks to clean up the Stinnes embarrassment; and possibly one or two other payments on Government account. The balance, therefore, represents the normal drain on the divisen account due to foreign commercial debt repayment and purchases of goods in foreign countries.

While the present position of the Reichsbank does in fact show a reserve of 58%, the theoretical position should be figured differently.

The law requires that the Rentenbank shall gradually retire its note issue, as I recall, at the rate of M. 120,000,000 per annum; and as those notes are retired, Reichsbank notes must be issued in exchange. The Rentenbank has M. 1,800,000,000 outstanding, making the total circulation of Rentenmarks and Reichsmarks M. 4,300,000,000. And in order to maintain the 40% reserve ultimately against what is at present "actual" circulation, the Reichsbank would need to hold M. 1,300,000,000 gold and 433,000,000 divisen. It will be seen that the Bank is some M. 200,000,000 short of gold, and is likely to be short of divisen unless the exchange should turn in Germany's favor.

The real difficulty about the note issue, therefore, is not apparent on the surface. The only way in which the Reichsbank can acquire gold in order to build up its 30% reserve is to convert divisen into gold, and the supply of

Reichsbank Position (cont'd)

divisen is being gradually, and until recently very rapidly, reduced by demands to pay for goods and to pay debts abroad. Therefore, the only way in which Dr. Schacht can maintain the reserve position of the Reichsbank will be to effect such a restriction upon credit (that is to say upon note issues) that his actual reserve requirements will constantly be reduced as his supply of divisen becomes reduced. It seems to be overlooked that this involves a reduction of M. 2,500,000 note issue to compensate for every loss of M. 1,000,000 divisen, - a somewhat similar position to that of the Federal Reserve System.

There is also a great deal of misunderstanding abroad as to the whole system of payments and reserves in Germany. The commercial banks do not carry large balances at the Reichsbank as the use of checks is exceedingly restricted and the 450 branches of the Reichsbank, which cover every part of Germany, give all the commercial banks and their branches ample facilities for getting notes whenever desired. They rely entirely upon the Reichsbank.

The system of payments (other than by bank notes) is entirely through the giro system. All large payments and financial payments are made through the giro system of the Reichsbank; and all small payments are made through the giro system of the post office. Before the war, the Reichsbank habitually required large balances as compensation for making giro payments. But the war imposed the necessity for an economy of credit which resulted in the Reichsbank instituting a system of cash charges instead of balances, which reduced the need for carrying balances at the Reichsbank; and the post office required simply a minimum balance as a general rule of only M. 5. The post office funds, nevertheless, on account of these deposits and other funds, aggregate over M. 500,000,000.

It will, therefore, be seen that the great bulk of the credit operations of the Reichsbank result in increases or decreases of the note issue, rather than in changes in the deposit account; and that the heavy burden of

Reichsbank Position (cont'd)

external payments, which depletes the bank's reserves, can only be effected under present conditions in case the bank is willing to impose such a restriction upon credit that they can reduce note liabilities at the rate of 2-1/2 times the loss of reserve.

Dr. Schacht tells us quite frankly (and stated the same thing to the Chancellor and to Mr. Stresseman) that he is looking forward to a very severe financial crisis in Germany because of this need for restriction of credit in order to maintain the external value of the mark. He is determined to maintain the value of the mark; and his only remedy is to curtail credit and keep the note issue down, - in fact to reduce it - though it will mean a very sharp reduction of prices throughout Germany, unemployment, and a social crisis.

In his latest conversations, however, he did say that if the German industrial establishments as a whole, including possibly German Municipalities in good credit, were successful over the next year in securing long time loans in America of from, say, \$200,000,000 to \$400,000,000, he thought he could see his way clear to maintaining stability, avoiding too serious a crisis, and giving the Dawes Plan a thorough-going, honest test.

Notes

#1. In a subsequent talk with Dr. Schacht, confirmed by Mr. Gilbert, I learn that the M. 45,000,000 paid in settlement of the herring account in Norway was paid out of the divisen held by the Government in a Government organization which had accumulated foreign exchange during the inflation period, and that, therefore, there was no reduction in the bank's reserve, but a gold gain of M. 22,500,000. Dr. Schacht intimated to me that the balance of divisen held by the Government was comparatively small, around M. 40,000,000; but that the Government had no further outstanding obligations abroad of any consequence to deal with.

#2. Further conversation with Dr. Schacht disclosed the fact that the Government is obliged to retire M. 60,000,000 of the M. 120,000,000 annual retirement of Rentenmarks, and the Rentenbank the other M. 60,000,000; and that in addition, all of the surplus profits which would go to the Government are applied to retirement of Rentenmarks, and even this does not consume all the profits of the Rentenbank, which has now accumulated

Reichsbank PositionNotes (cont'd)

a capital out of earnings of M. 200,000,000, which, by the end of the year will probably be M. 250,000,000 (Rentenmarks)

Stinnes Affair:

The information I gathered about this came chiefly from Dr. Schacht, so from Mr. Von Siemens and a few others with whom I discussed it.

It seems that a few months ago young Hugo Stinnes, being the younger brother, came to Dr. Schacht with a request for assistance to the extent of M.90,000,000 or M.95,000,000, stating that he owed M.150,000,000, largely representing short time obligations given for the purchase of properties. I judge these were acquired mainly since his father's death. He and his brother had had disputes and they had decided to separate. There seems to be some doubt as to who was responsible for the fiasco, and as to which of the brothers, if either, had the brains. Hugo is quite a young man, under thirty, and undoubtedly not qualified by experience or ability to deal with the enormous situation which was left by his father.

It seems that the M.150,00,000 had largely been furnished by German banks, some having been borrowed abroad. Dr. Schacht told Stinnes that he regarded the German banks who had facilitated his transactions as equally guilty with him in a very unwise speculation, and that he would do nothing whatever to assist them; that he must get the bankers together and work out a plan with them.

It resulted in a meeting at the Reichsbank, attended by some twenty-five bankers. I guess Dr. Schacht gave them a good combing, and they then agreed to extend the maturing loans, which he found, on inquiry, were not M.95,000,000 but M.120,000,000, the other M.30,000,000 representing foreign borrowings which were maturing. And Dr. Schacht required the bankers to put up the money with which to buy divisen from the Reichsbank so as to pay off the foreign obligations and thus avoid the shock to German credit which would have resulted.

Dr. Schacht says that the situation is not as bad as it appears to be. In the first place, there will be no losses to either the banks or the public, the only loss being a very large shrinkage in Stinnes' equities. He had figured his net worth at some M.350,000,000. They are now proposing to sell off these properties as rapidly as possible, in fact some have already been sold to pay

Stinnes Affair (continued)

off Stinnes's obligations out of the proceeds, and he believes it will leave Stinnes a fortune of from M.50,000,000 to M.100,000,000, or even more, but will put him entirely out of the situation as a disturber.

Dr. Schacht was a good deal disturbed by some slight evidence of bad faith on young Stinnes's part. It seems he went over to London, without a word to Dr. Schacht about it, where he met Clarence Dillon, who offered to let him have M.80,000,000 (say \$20,000,000) to clean up the affair, provided the German banks would take care of the balance with second liens. Dr. Schacht said it was no situation to justify borrowing abroad, nor did the situation justify allowing this young man any possible way of again getting into trouble.

From what Colonel Logan said to me in London, I gather that Dillon felt that some of the German bankers were trying to squeeze Stinnes a bit and make a killing out of the wreckage. Dr. Schacht gave me quite a different impression; in fact that he was not proposing to have large credits arranged abroad to a weak borrower, which would later cause trouble, but would rather clean the situation up once and for all, and within Germany.

There was some amusing discussion of this at luncheon at the British Embassy, when Lord D'Albernon asked Dr. Schacht about the Esplanade Hotel in Berlin, which he had heard was being sold, and which was one of the seven or eight hotels that Stinnes owned. Dr. Schacht stated that he thought all the hotels had cost about 2,000,000 sterling, but that they could be purchased now from the Stinnes creditors for 1,000,000 sterling, this notwithstanding the fact that real estate values have had a great advance recently. One evidence is the situation as to our own Embassy in Berlin. It is a large house on Wilhelm Platz. Mr. Gerard paid a rental of M.4,000 gold originally for the place. The rent was advanced once or twice until recently it got up to M.15,000 gold. And Dr. Schurman told me it was owned by one of the banks which wished to turn it over to the President of the bank as his official residence, so that in order to obtain an

Stinnes Affair (continued)

extension for a year, he would probably have to pay a rental of M.75,000.

On the whole, it struck me that the Stinnes affair had been handled conservatively and well, and that it was much better to have it cleaned up as Dr. Schacht proposed, than to have it the subject of some foreign exploitation. Dr. Schacht said that two weeks now would see it all in good shape, with young Stinnes so under control that he would have to behave himself.

RAILROAD SITUATION IN GERMANY

Considerable uncertainty seems to exist as to the outlook for the railroad system.

I finally had an opportunity for a long talk with the Frenchman who is in charge, a Mr. Gaston Leverage, who, from Gilbert and others, I learned is very highly regarded indeed, and, indeed, he made a most favorable impression upon me, - as have all of those connected with the Dawes Organization in Berlin.

Under the Dawes Plan, of course, the railroads have been detached from Government control. The Government no longer finances them, and they are obliged to rely upon their own resources for the maintenance of property, which is done out of earnings. This year the charge on the railroad earnings for the Dawes Plan service is M.200,000,000; next year M.600,000,000.

The general impression abroad seems to be that the railroad lines are in perfect condition. Mr. Leverage tells me that they are over-supplied with equipment, both locomotives and cars, which is in fair condition, although the passenger equipment needs overhauling. He says that some of the main lines, like the one we took from the Hook of Holland through Holland to Berlin, are in excellent condition, as is the line to the Belgian frontier, going to Paris. But many of the lines need road work rather badly, and it will be some time before they can be brought up to the condition they should be in. They are considerably over-manned with personnel still. The pension system is now so heavy that there is strong inducement to retain in active service a good many of the older, less efficient men, and get what work out of them is possible, rather than let them go and employ more active men, with the double cost of wages and pension.

Mr. Leverage says the Germans are urging expenditure of money on the lines constantly so that when they ultimately revert to the Government they will be in apple pie order. He is proposing a certain amount of expenditure, but

thinks that their claims are extravagant.

Unfortunately, a dispute has recently arisen between the Dutch and the Germans in regard to railroad rates, which caused Dr. Schacht a good deal of embarrassment. It seems that prior to the war the German Government had built some kind of canal waterway along the Dutch frontier so as to avoid routing a considerable part of the railway freight to Dutch ports for shipment to America and elsewhere. Work was suspended because of the war. Quite recently a rearrangement of rates and routing was effected, by which a large part of the freight traffic for port shipment was diverted to German ports, thereby depriving the Dutch railways of the earnings. Without any preliminary word to Dr. Schacht, Dr. Vissering sent a circular letter to all the Dutch banks advising them that in view of the discrimination against the Dutch railways, he thought it would be inadvisable to continue German credits. This did, in effect, result in a large withdrawal of credits and quite a strain on the Reichsbank foreign balances. Those that were not entirely discontinued were reduced to 30% or 40% of normal. Dr. Schacht learned of it only through some banker, who sent him a copy of Vissering's letter. Of course, as a matter of fact, the German Government had nothing to do with it, the arrangement was made by the railroad management, - now divorced from the Government - and was done in the interest of larger earnings, as Lerverve told me himself. But it made a very bad impression, and is another one of those acts of retaliation which is taking place all over Europe. Mr. Max Warburg and Mr. ter Meulen, of Hope and Company, have taken the matter up in Holland, and they are hopeful that a satisfactory adjustment with Vissering and the bankers can be effected. But the situation has been, nevertheless, a little strained.

7/22 d

DISCUSSION AT REICHSBANK LUNCHEON

SATURDAY, JULY 11, 1925

Dr. Schacht, Dr. Luther, Mr. Stresseman

We had a long discussion at the table of economic conditions in Germany, which will be covered in another part of my memorandum and I shall not repeat here.

After luncheon Dr. Luther and I had a long talk about the outlook and the American attitude toward German finances, etc.

He first stated that the valorization plan now being dealt with by the Reichstag was absolutely imposed upon them by an urgent public opinion, supported by the severe poverty of the middle classes, who had lost all of their savings by the wiping out of public and private debts in which their funds were invested. They had to do something about it as public opinion was almost unanimous in requiring it.

The proposal now before the Reichstag, which he thought would pass in substantially this form, contemplates that mortgage debts of private concerns shall be revived at 25% of their nominal face amount, interest starting to be paid at a low rate, say 3%, and increasing until in 1927 it would be 5%. These private mortgage debts would also include certain land mortgage savings obligations in which the very poor classes have lost heavily.

(Dr. Schacht subsequently said that he understood that, as to these private mortgage debts, new money would be allowed to take priority over the valorized debt.)

The Government debt would be revived at 5% of its nominal value in the case of debt remaining in the hands of those who had acquired it prior to July 1, 1920. And as to holders of the debt subsequent to July 1, 1920, they would receive 2-1/2%. The debt revived at 5% (that is the class prior to July 1, 1920) would bear 5% interest, commencing some time next year, whereas

the 2-1/2% debt would bear no interest. The payment of the principal of this debt, I gather, is deferred in some way until a subsequent date related to the operation of the Dawes Plan, but that was not mentioned specifically.

Of course the revival of this debt, so far as it is held abroad, will impose some strain upon transfers whenever the time comes for the payment of interest or principal, and Governor Norman also feels that it will create a great outcry in England, where a good many German Government obligations are held, because trading in the German Government bonds on the stock exchange has been conducted as though it were all of equal status and value, and if this valorization scheme goes through, it will be found that they were really trading in two different classes of German bonds without being aware of it, and it may give rise to a good deal of criticism and disorder.

I think this is hardly justified when one considers that the period of inflation commencing about July 1920 resulted in purchasers of German Government bonds subsequent thereto getting them at a nominal cost, so that even the 2-1/2% will mean a profit; whereas those who held them continuously since before July 1920 probably paid a good deal more for them, and most of them, even at 5%, will realize only a fraction of their investment.

Dr. Luther then launched into a general discussion of the pact and the question of political tranquility in middle Europe. I pointed out to him that the attitude of financial people in America toward Germany, and toward Europe generally, would be very much governed by the degree to which confidence was felt in political conditions. I reviewed somewhat the history of what had happened at the time of the decision not to evacuate the Cologne area, the Ruhr and the cities of Dusseldorf, Duisberg and Rhurort, stating that every time developments of that sort occurred, and every time anything like a disclosure such as that made by the Military Control Commission appeared, it sent a chill over the financial community at home, and made it exceedingly difficult indeed for any of the affected parties to place loans in America.

That, he said, in his opinion, struck at the root of the whole problem of recovery. Without political security, and confidence in it abroad, Europe was going to have a hard time.

I asked him what the prospects were of something coming out of the pact, and he said that they had submitted to the French a very simple, concrete proposal, embodying simply the principles, which he felt had a good deal of support in England; that the French reply was a highly technical, legalistic document, exceedingly difficult to answer, and especially to answer so as not to give the impression that Germany was balking peace. He said it never would be possible to accept some of the conditions laid down by the French, but he, nevertheless, was hopeful of a satisfactory outcome of the negotiations, and that they were working diligently on an answer which would be dispatched, he hoped, in about a week.

I explained to him that I had no connection whatever with political affairs and was interested in them simply as being one of the conditions which affected the operations of the banks of issue, and especially the relations which we might endeavor to maintain with similar institutions abroad, like the Reichsbank and the Bank of England. He said this he understood perfectly and why I was interested in discussing the question of the pact.

I asked him then, simply as a personal inquiry, whether it might not be that the German reply would be of a character that could be misunderstood, or misinterpreted as indicating that Germany again was evading a move toward real peace. And he said that the facts were so contrary to that, that he felt that it could be met. He said there is nothing that Germany so eagerly and keenly desires as a real peace with all of her neighbors; not only that, but they were fully convinced of the disinterested impartiality of the Dawes Plan, and were hoping that the French would give them opportunity to make a serious effort to carry it out in its entirety; but that if they could not have security on their frontiers, it would be very dif-

Berlin

difficult for Germany to reestablish her credit throughout the world and gain the aid which is urgently needed.

He expressed himself as delighted that I had made the trip to Berlin, and said that anything and everything that I needed in the way of aid or information was at my command.

I had very little talk with Mr. Stresseman.

RECEIVED
ECON
7/11/25

LIST OF GUESTS AT DR. SCHACHT'S LUNCHEON

July 13, 1925.

Herr Bankier Fritz Andreae	Fa. Hardy & Co. G.m.b.H. Berlin W. 56 Markgrafenstr. 36
Herr Geheimrat Bernhard	Reichsbank, Berlin
Herr Professor Dr. Bruins	Reichsbank, Berlin
Herr Geheimrat Budczies	Reichsbank, Berlin
Herr Reichsbankdirektor Dreyse	Reichsbank, Berlin
Herr Geheimrat Friedrich	Reichsbank, Berlin
Herr Reichsbankdirektor Fuchs	Reichsbank, Berlin
Herr Hans Furstenberg	Geschäftsinhaber der Berliner Handelsgesellschaft, Berlin, W. 8 Behrenstr. 32/33
Exzellenz v. Glasenapp	Reichsbank, Berlin
Herr Jakob Goldschmidt	Geschäftsinhaber der Darmstädter-u. Nationalbank, Kom.-Ges.a.Aktien, Berlin, W. 8 Behrenstr 68/69
Herr Carl Joerger	Delbruck, Schickler & Co., Berlin W. 66 Mauerstr. 61/65
Herr Vizepräsident Kauffmann	Reichsbank, Berlin
Herr Franz v. Mendelssohn	Fa. Mendelssohn & Co., Berlin W. 56 Jagerstr 49/50
Herr Direktor Nathan	Dresdner Bank, Berlin W. 8 Behrenstr.
Herr Direktor Sobernheim	Commerz-u. Privatbank Berlin W. 8 Behrenstr 46/48
Herr Geheimrat Schneider	Reichsbank, Berlin
Herr Bankier Paul v. Schwabach	Fa. S. Bleichroder, Berlin, W. 8
Herr Franz Urbig	Direction der Disconto-Gesellschaft, Berlin W 8

(over)

Spa, Belgium

FEDERAL RESERVE BANK OF NEW YORK 7.24.25 - List of Guests at Dr. Schacht's Luncheon
July 13, 1925, Continued

(2)

Herr Geheimrat Vocke	Reichsbank, Berlin
Herr Prasident Wagemann	Statistisches Reichsamt, Berlin W. 10 Lutzowufer 6-8
Herr Staatssekretar Weismann	Preuss. Staatsministerium, Berlin W. 8 Wilhelmstr. 63/64
Herr Kommerzienrat Millington-Hermann	Deutsche Bank, Berlin W. 8
Herr Professor Bonn	Berlin W. Landgrafenstr. 6
Herr Gert Weismann	Sekretar des Herrn Prasidenten Dr. Schacht, Reichsbank, Berlin.

WELCHER
BUND
HEWNEBRIEF

Berlin, Germany,
July 11, 1925.

Dear Pierre:

It was my hope to be able to sandwich in a half day here and there when it would be possible to write you some fairly long letters which, together, might form something of a narrative of my visits. But so far there has not been a moment to spare beyond what I took to write you from London. I shall, however, make some notes, and those can later be worked up into something of a narrative. Dr. Stewart is doing the same.

Aside from visits with the folks whom you would expect at the Bank in London, I had one very nice talk with the Prime Minister, also a visit with Gaspard Farrar of Barings, who, as you know, is an old friend; and two long visits with Mr. Houghton. The last was most interesting, as he gave me a very illuminating account of the political situation in Germany. In fact he went out of his way, after we had spent a morning together, to finish up by a couple of hours at his house late one afternoon. It gave me a fine approach to our talks with Dr. Schacht.

We all left London by the 8:30 p. m. train on Wednesday (and when I say all, I include a formidable array of luggage as well); crossed to the Hook of Holland that night and took the train there at 7:07 a. m. on Thursday; arriving promptly in Berlin at 5:40 p. m. Thursday, after a very comfortable trip. Dr. Schacht, Mr. Gilbert, and Mr. Sterrett were at the station to meet us. In fact, from the time we left England until we reached the Adlon Hotel, everything possible was done to make the trip easy as to passports, luggage, etc. They had reserved a magnificent suite for us at the Adlon, the coincidence being that they are the same rooms that I had here in 1914.

Thursday evening we all dined with the Gilberts.

Friday morning Norman and I went to the Reichsbank, and never left until after 7:00 o'clock.

And I am dictating this late Saturday afternoon after spending the entire day at the Bank again.

Last night we dined with Dr. Schacht, and he had one of his men, Dr. Bruins, there also, and Mr. Heineman of Brussels, whom I think you know, then Norman, Stewart and myself. Today the luncheon party at the Bank consisted of the Chancellor, Dr. Luther, and the Minister of Foreign Finance, Mr. Stresseman. Tonight some of us are dining with the Sterretts, but I am going off with Mr. and Mrs. Morgan, and likely Dr. Stewart will go with us, for a little family confab.

Berlin, 7.11.25.

It seems a shame to write you at all and not give you something in the way of information, but I really think it will be better to wait until I have gotten it written out and corrected, and in something like orderly shape.

On the way to the Bank this morning I stopped to pay my respects to our Ambassador, Mr. Schurman, who, as you know, is an old friend. And he literally grabbed me, insisting that I should stay long enough to have one or two visits with him to talk over various things; he having just taken up his post, and, I imagine, feeling considerably at sea.

The trip to Spa is fading away into the dim distance, not because we have abandoned the idea of a holiday, but because everyone unites in saying that Spa is the wettest place in Europe, where you never see the sun, and I told Norman that I wouldn't go to such a place. I am not sure now where we will go.

We all keep well, and Mrs. Humphrey seems to be having a grand time out of the trip, although I have abandoned her to her fate, and to some of my friends.

Please give my best regards to everyone at the bank.

If I get that skeleton from Harrison pretty soon, I can do some work on it while on our holiday.

The enclosed clippings speak for themselves. The only one for which I accept any responsibility is the one from the Berliner Borsen-Courier, which was edited at the Reichsbank and given out by Dr. Schacht.

Very sincerely yours,

Pierre Jay, Esq.,
Chairman, Federal Reserve Bank of New York,
33 Liberty Street, New York.

FEDERAL RESERVE BANK
OF NEW YORK

Berlin, Germany,
July 15, 1925.

Reichsbank
ANSWERED
AUG 7 1926
U. S. F. B. N.Y.
[Handwritten signatures]

*copy forwarded to Mr. Case
7/25/25*

Dear Mr. Case:

My last letter went to Mr. Jay, and I overlooked the fact that it would arrive during his absence. I am not sure whether Miss Holmes would have opened it or not, so I am enclosing a tissue copy of it.

Enclosed are a couple of newspaper clippings, in one of which you will observe that our friend Willis is still taking a hand in misrepresenting us before the public in his usual, graceful style.

And separately I am sending four copies of the report of the Agent General for Reparation Payments, which will be a good thing to have in the library. It gives an excellent account of matters bearing on transfers, etc, and it has made a very good impression here. Gilbert is exceedingly well regarded, and has established himself in everybody's confidence.

We have been so exceedingly busy trying to get all the facts bearing on the position of the Reichsbank and the monetary and credit situation, that I have not been able to keep up even with my notes. However, we are leaving Friday night for Spa, and there I hope to reduce all of this material to something like a workable account of our trip to date, and I will send a copy to you. Of course it must be held in strict confidence, as much of the material is given to us very confidentially indeed. I will try and mark those portions which should be so considered.

Dr. Schacht has been the most hospitable possible host; has answered all of our questions with frankness; and has volunteered a good deal of information which could not have been had from anyone else. We have spent practically all of our time at the Bank, but have also had opportunity to meet the Chancellor and some of his Cabinet; as well as the British and American Ambassadors; and, of course, Gilbert and his organization. Then one night we met ten or twelve of the leading bankers at Dr. Schacht's, after a small dinner party.

I must still defer giving you anything in the way of an account of how things are here until the material is arranged.

Dr. Stewart is busy every day working along separate lines, and he will also have some interesting material. As he will not remain as long as I shall, we have arranged for him to go to Amsterdam to meet Dr. Vissering, while we are at Spa. Then he proposes to return to London and finish up his work there; and to join me later in Paris.

*delivered to
Wray
8/2*

Meantime, I will have had a chance to visit Brussels, and possibly Amsterdam. But it may be that I shall skip Amsterdam in case Dr. Vissering goes to London later.

The trip to Prague, Budapest, and Vienna seems to be a luxury that I cannot afford without being away too long. It would take ten days at least, and I think it is exceedingly important that I should be in London at the time when Governor Norman is expecting the commencement of the exchange pressure. One hopeful outlook is the excellent crop which Germany seems certain to make this year; but there are other dangers in the exchange situation which are going to be very difficult indeed.

I am enclosing an interesting exhibit of the presence ^{and} large number of the fonctionaire. It is a manifest, or bill of lading, representing the shipment of some small article that Shepard Morgan purchased in Paris, and covers only the trip from the frontier to Berlin. The other part of the bill of lading (from Paris to the frontier) I understand was similar to this in appearance. You will notice that it has fourteen separate stamps on it, and each stamp represents some kind of entry in a set of books. All of this, apparently, had to be paid out of a transportation charge of M. 11:55. I understand that the same condition of over-organization resulting from the period of inflation is present generally in the commercial, industrial, and transportation establishments.

Please give my best to all the folks at the Bank, and the same to you. We all keep well, but I am frank to say that we are pretty well exhausted after the strenuous days here.

Sincerely,

J. H. Case

J. H. Case, Esq.,
Deputy Governor,
Federal Reserve Bank of New York,
33 Liberty Street, New York.

Encs.

MAKING THE DAWES PLAN SURE

Berlin Tageblatt
July 14, 1925.
Washington. *July 15*

The Berlin Consultations of the Bank Presidents

The Philadelphia Public Ledger to-day points out the great significance of the present Berlin consultations of Bank Governors Strong and Norman. "It is clear," writes the newspaper, "that these leading financial authorities do not intend to inform each other about weather conditions or turtle-eggs from Timbuctoo, but are preparing decisions of the greatest importance for the financial fate of the world." The making sure of the Dawes plan stands in the foreground of interest and the necessary preparatory measures for this must be taken at the right time. The present Berlin conferences will be followed by numerous ones of similar nature till conditions attain a common definite stabilization.

- 0 -

Vossische Zeitung
New York, July 13.

AMERICA ON THE VISIT OF THE BANK PRESIDENTS

The visit of Norman and Strong to Schacht has interested greatly the New York Banking circles. The most varying versions as to its object are in circulation. The simplest explanation is that Germany seeks an additional loan to the Dawes loan. The second explanation is England is so embarrassed by the return to the gold standard that she needs for herself the resources which she formerly placed at Germany's disposal, and that account Strong wishes to inform himself, in order to come to England's assistance. This would especially concern a German short-term credit affair and the exchange discount. The third version, finally, asserts that, in connection with the transfer question, the foundation of branches of the combined general Reserve banks in Germany and perhaps in England also, is planned.

- 0 -

Berlin Tageblatt
Washington, July 13.

AMERICA AND THE TRANSFER QUESTION

The leading New York commercial newspaper, "Journal of Commerce", speaks under the heading "Mysterious Finance", of the Berlin journey of the Governor of the Federal Reserve Bank in New York, Strong, in company of the Governor of the Bank of England, and writes: "Since England has returned to the gold standard, it is no longer able to hold Germany under the arms with credits as liberally as before, and America's help is therefore necessary for the solution of all the currency problems that arise in connection with the carrying out of the Dawes plan. Difficulties of transfers could only be overcome by securing short-term credits. In this it is a question of technical transactions, the carrying out of which would be not at all in contradiction with the American policy of keeping away from the entanglements of the Reparations question." The newspaper demands that all necessary bank operations in this connection should be carried out on a strictly legal basis, in order that there should not again be a protest of the American Congress, as there was in the case of the restoration of the English currency to the gold standard. America has every interest in Germany's returning to sound currency conditions, as England has.

- 0 -

Frankfurter Zeitung
July 12.

INTERVIEW OF THE NOTE BANKS

Our Berlin correspondent writes: "It is undoubted testimony of a great moral success of the young Reichsbank, that it could receive the visit of two leading note bank heads, two persons, to wit, who are not imbued with the quality of controllers or of creditors, but are simply the representatives of the currency banks of their countries and as such wished to confer with the currency bank of another country. Mr. Scron (Strong) of the Federal Reserve Bank of the State of New York came, on his European journey, to the Bank of England, and the lately re-elected

Governor Norman of that bank, for a long time conversant with German problems and German personalities, accompanied him on a journey to Berlin. Apparently the visit had no practical business or currency-tactics object, but instead the purpose of drawing closer the present contact, and of talking over all subjects which to-day can interest the note bank heads of important countries that are related to each other in the general rearrangement of world and money economics. Among those the Transfer problem and the questions for the year 1926 are said to have been discussed. The conference lasted many hours and the parting was in a very cordial tone, if a chance observer might judge. They clearly gave each other full information, especially was that done from the German side and conscientiously; they undoubtedly agreed unanimously in their views and in the currency policy; only in this way can mutual understanding be secured for the case, that some time later - not now - international financial questions of importance may be solved by mutual consent. To speak of credits and loans as a subject for the conference is naturally absurd. It is amply sufficient when the guests carry away with them a good impression of the commonsense with which bank policy here is handled, and of the earnestness with which German industry is striving to bring about its reformation and its readaptation. From convictions obtained personally alone can support be found for German private credit abroad, which later, especially when lands come into contact again, are of greater use than any present agreements, which would have to count on the difficulties of foreign markets.

FEDERAL RESERVE BANK
OF NEW YORK

Spa, Belgium,
July 19, 1925.

Dear Mr. Jay:

Many thanks for your nice letter of July 3.

I am not surprised at what you write about Kansas City. That district, and California, need stirring up on member bank relations as much as any, and I hope your committee can get them started.

Traylor's interview struck me as excellent. I should think he would arrange for its use in Chicago as that's where it would do most good.

My understanding of the charter plan is that if agitation continues for recharter, amendments, etc., Congress be asked to pass a recharter bill right away, and take up the amendments later. This was the matter that Stewart and I cabled you about, and there isn't much to add to that. I do think the scheme is an excellent one if the subject of recharter must be dealt with at the next Congress.

I have read Willis' article, which was cabled to Germany and published there; also the Whaley Eaton article. Doubtless the rumors have to do with what I heard. If the Journal of Commerce should be sold, I surmise that Willis may not have such easy sledding.

I am enclosing another batch of Berlin clippings, which, in point of fact, I have not had translated to me as they came just as I was leaving. So I don't know just what they do contain, and won't bother here to find out. Can you have the translations of them kept out for my return?

Won't you also thank Dr. Burgess for his memorandum of July 3, which I have read with interest. I shall be glad to have others as occasion suggests them.

Unquestionably our visit to Berlin made quite a stir, for all sorts of rumors were about. But, having consulted with Gilbert and some others, I concluded that it would be dangerous and unwise to see the American correspondents. This was principally because of the personnel. Upon their advice, however, and learning that he was thoroughly dependable, I did have quite a talk with Endres, the Berlin representative of the Associated Press. I explained to him first that Melvil Stone and Kent Cooper were warm personal friends of mine, and that I frequently see them and talk over banking matters with them; that I could give no interview whatever. And he agreed that he would not use my name, or permit it to be used at home. Then I told him that I had not come to Germany to tell the German Government, or the Reichsbank, or Mr. Gilbert, or anybody else, how they should run their business; nor had I come in connection with any credit or other special transaction; nor to open a branch of the Federal Reserve Bank; nor to check up the Reichsbank's accounts, or Mr. Gilbert's; nor to buy bills; in fact to do none of the various ridiculous things which rumor suggested were in the wind. I told him that the Reichsbank had had close relations with us for some time past, and that I had simply come to make Dr. Schacht's acquaintance, and to learn from him something of conditions in Germany, especially as to banking

Recharter
ANSWERED
JUL 27 1925
U. H. C.

Being held for
How strong
return
H. C. Burke

3/3/25

Spa, July 19, 1925.

and monetary matters, and that this was in line with what seemed to be a perfectly natural, normal, and spontaneous development since the war in the gradual drawing together of the banks of issue for the sake of mutual understandings. In fact it was quite likely that I would do something of that sort every year hereafter, and I was hoping that the heads of some of the central banks of Europe would visit New York in like fashion. I pointed out to him that the gradual move towards resumption of gold payment in Europe made it exceedingly necessary that we should have first hand information and personal acquaintance with the men with whom we would need to deal as these monetary questions developed in importance and activity.

We then had a general chat about conditions in Germany, and he gave me some interesting news about various personalities.

He agreed to advise his people at home in such a way that I would not be quoted in any way.

We got completely exhausted in Berlin with protracted meetings which lasted all day long, usually with a rather tedious, typical, German lunch in the middle of the day, and a dinner every night. So we left Friday night for Spa as planned, reaching here Saturday noon. Since then we have been resting, most of the time in bed, and today, Sunday, I am just beginning to come to life again.

Norman impresses me as being completely exhausted, which is not surprising, for I find he has been through a terrific strain, and, of course, he is still inadequately supported at the Bank.

Most of what I want to send you will appear in a long memorandum which is in course of preparation, but the completion of which will necessarily be delayed a few days as it is quite a job.

I am sending you with this, however, some separate letters to the officers of the bank on subjects which seem to require some consideration right away, and on each of which I would very much appreciate frank comment by letter or cable as indicated in each separate letter.

When I can get around to it, I will also send a list of the bankers I met at luncheon on July 13th, given by Dr. Schacht.

Won't you give my best to everybody at the bank. I was overjoyed to get too all the bundles of reports with your letter and some others, but I must ask you all to be patient about replies for about a week or so.

Very sincerely yours,

Benjamin Strong

Rentenbank Credit
JUL 27 1925
D. H. C.

FEDERAL RESERVE BANK
OF NEW YORK

PERSONAL & CONFIDENTIAL

Spa, Belgium,
July 20, 1925.

Dear Mr. Jay:

I have written Mr. Kenzel about one credit matter concerning which Dr. Schacht spoke to me, and this relates to another credit which I believe is of considerable importance.

It seems that some time ago Harris, Forbes & Company had tentatively negotiated a credit for one of the agricultural loan institutions, to be secured by mortgages on farms. Subsequently, a representative of the National City Company (or the National City Bank) approached Dr. Schacht with the suggestion that they might consider making a loan to the Rentenbank. Dr. Schacht succeeded in convincing the representative of Harris, Forbes & Company, as well as the City Company's man, that they should join hands in the transaction, and that it should take the form of an issue for the Rentenbank.

The matter had reached a point where the maximum amount of the loan had been discussed as \$100,000,000, a portion only to be issued at first. The rate of interest had been almost agreed upon, being somewhere, as I recall, between 8 - 9%. And I gathered from Dr. Schacht's statement that they were pretty close to an understanding as to the form of security, etc.

The status of the Rentenbank I gather to be as follows:

Upon the reorganization of the Reichsbank, this was promptly converted into an agricultural credit bank, and loans made by the Reichsbank (which were somewhat in exception to their general policy) to the farmers of Germany, secured by farm liens, were transferred to the Rentenbank to a total of some M.700,000,000 or M.800,000,000. All the details of the transaction are not clear to me, but the result is that the portfolio of the Rentenbank now largely consists of these farm mortgage loans.

Dr. Schacht tells me that the business is very profitable, their discount rate of 7% being, of course, a concession to the rather urgent needs of agriculture for increasing production and reducing costs.

The capital is, in round figures, M.200,000,000, most of which, I believe, has been earned. The earnings are now very heavy.

Under the law resulting from the Dawes Plan, the circulation of the Rentenbank, which is M. 1,800,000,000, must be retired at the rate of M.120,000,000 a year, M.60,000,000 by the Rentenbank, and M.60,000,000 by the Reich. Over and above the M.120,000,000 the Rentenbank pays large profits to the Reich out of surplus earnings, and these, I believe, are likewise applied to retire the Rentenmarks. But even with these payments Dr. Schacht says that they will add M.50,000,000 this year to their capital and reserve out of earnings.

In order that the Rentenbank may function more as an agricultural credit bank, and, of course, in time retire as a bank of issue, a bill is now pending in

the Reichstag providing for a reorganization of the Bank. It is expected to pass almost any day. It is intended to fill the gap in their economic machinery in such a way that the agricultural community can get credit which is badly needed; lack of credit being one of the outstanding deficiencies in the German position just now.

From what Dr. Schacht tells me, I should suppose that it would not be difficult to arrange a well secured loan for the Rentenbank, which might indeed sell quite well at home. The loan would be secured, I gather, by a statutory lien of 6%, the same as the Rentenmark, upon all farms in Germany having a value in excess of M.6,000. In addition to that, the individual farmers would be able to make mortgages, as I recall, up to a maximum of 25% of the value of the farm.

Now of course it must be borne in mind that there are certain specific points requiring careful investigation in connection with any such loan. These, nor in fact many other features of the business, could not be studied by me while in Berlin as time did not permit. But I can, at least, give a rough description of their significance:

(1) The Dawes Plan priorities as to foreign payments might be capable of being construed as coming ahead of all private payments, and, therefore, if the operation of the Dawes Plan became wholly unsuccessful and transfers could not be made without encroaching upon supplies of exchange for making private payments, will the Agent General at any time insist that private payments be allowed to default in order that the Dawes Plan payments may be made?

This is the same story we have so often heard, and Gilbert tells me that he is unable to give any assurances to anybody on that subject. I think he is quite right. But the general provisions of the Plan in regard to the maintenance of German economic integrity afford some protection, and certainly the ability of citizens to borrow abroad for such a necessary purpose as the maintenance of agricultural production can hardly be construed as wastage of resources.

(2) The mortgage lien of the Dawes Plan, I gather, will not affect the farmers. But that, of course, needs to be investigated and understood.

(3) The valorization law, which has passed, or is just about to pass the Reichstag, will likely have the effect of reviving 25% of the nominal value of mortgages on farms in Germany. And any such decision, without careful study, would make it very difficult to determine exactly what position new loans will occupy.

My suggestion would be that anyone making a loan to the Rentenbank would need to inquire, first, as to the Rentenbank lien for security of the Renten mark; second, as to the Dawes Plan lien for the security of the Dawes Plan payments; third, as to the valorization lien of revived mortgages; and, fourth, as to the general position of the Rentenbank, - the appropriation of its capital, and whether the capital must be maintained in its integrity after the new law passes.

As stated above, I doubt if anything can be done in the way of assurances as to Dawes Plan transfers.

Now I have told Dr. Schacht that it seemed to me that he was wise in securing a consolidation of the negotiations with these different concerns; that

he was in thoroughly responsible hands in dealing with them; and that were I at home I would not hesitate to tell Mr. Mitchell that my impressions were quite favorable, with the understanding, of course, that all of these matters would be the subject of careful investigation and study, which doubtless has already been made. It may be that investigation will show that the legislation provides for a determination of the relations of the various liens, so that some of the questions mentioned above will all be resolved by an examination of the law itself.

I am told by Gilbert, however, that these loans in America should only be made anyway after careful advice as to the statutory position, because this is sometimes complicated and requires the study of people who are fully informed.

As Germany needs long credits, and certainly cannot afford the hazard of short credits, this is the kind of business which will be of real benefit. The security is so diversified and the agricultural situation in Germany is now so settled that my surmise would be that the loan would have ample security. The crop, this year, appears to be in first class condition. As to that all reports agree. A large part of it is beyond the point where any damage can be done. The weather just now is perfect for the maturing crops, and I should suppose that a fortnight or a little longer would see them all safely matured, including oats.

There is one thing, however, which should be mentioned in this connection. The whole economic and industrial situation in Germany is approaching a crisis due to the shortage of credit, the policy of restriction imposed by the Reichsbank, and the need of eliminating the mushroom growth of weak, poorly organized and under-capitalized enterprises, which simply add to the cost of distributing the product of the nation's industries. There is also great need for a period of economy in wasteful expenditure. The period of inflation led to such distrust of the paper currency, that people cultivated habits of spending it directly they got it. These habits have not yet been cured, and cannot be until after Germany has had some housecleaning.

This Dr. Schacht has reiterated to me repeatedly. He made the statement frankly before Luther and Stressemann. And later I had opportunity to talk it all over with Mr. Von Siemens, who stated to me almost exactly what Dr. Schacht had said.

Upon inquiry of various people, I find that Mr. Von Siemens is one of the most respected men in Germany. He is the head of the big Siemens electrical properties, employing about 100,000 men in their plants around Berlin. And I found him one of the most delightful men I have met. Mr. Young can tell you something about him. I would rank his opinion very highly.

So you see the difficulties about the business are partly technical, and partly those which will arise due to some crisis in Germany which might temporarily discredit German industrial and other private borrowings abroad. It would be a purging process which Germany needs, and from which she will probably benefit.

Were I at home, I would have a talk with Mitchell quite frankly about all of this, and, without assuming any responsibility, I think my attitude would be

conservatively to encourage him to go ahead.

If you do have a talk with him about it, I wish you would cable me quite fully the result, and I will be glad to help with Dr. Schacht in any way that I can within the limits of propriety.

Incidentally to this, provided Warburg agrees to the general ideas expressed in my letter to Kenzel, it might not be improper to say something to Mitchell also about the Gold Discount paper, as I believe his representative made some inquiries of Dr. Schacht about the possibilities of handling some of that in New York.

In general, I do not think it will do any good, and possibly may do harm, to have these credits negotiated in America at rates lower than credit conditions in Germany now justify. The ordinary commercial borrowers are paying as high as 12% for accommodation; the Reichsbank rate is 9% for bills, and higher than that for Lombard loans, of which they make very few indeed; and the Rentenbank rate is 7%, being a special concession to agriculture.

Sincerely,

Wm. H. Wood

Pierre Jay, Esq.,
Chairman, Federal Reserve Bank,
33 Liberty Street, New York.

*Recd by [unclear] 8/11/25
JWB*

ep
AUG 7 1925
J. H. G.

FEDERAL RESERVE BANK
OF NEW YORK

PERSONAL & CONFIDENTIAL

Spa, Belgium,
July 20, 1925.

Dear Mr. Jay:

As you know, I reached Berlin on the afternoon of July 9. We spent all day Friday and all day Saturday in discussion with Dr. Schacht. On Sunday we rested. And then, with only the interruption of intermittent visits with Gilbert, Morgan and Sterrett, and some others, we spent all of the time until last Friday night in a similar way.

I fear Dr. Schacht gained the impression that he was being pretty thoroughly combed. We covered every conceivable subject, and, at the end of it, I am frank to say that I cannot find a flaw in his attitude, with only a few minor exceptions:

One is that he is undoubtedly an exceedingly vain man. This does not so much take the form of boastfulness, as it does a certain naïve self-assurance. Another is that he has something the fault of a crusader. He believes that his program will not succeed unless people understand it, so he bursts out into speeches every now and then, and, in these, occasionally, gets into political matters which would be better left alone by the head of the Reichsbank. An illustration, - and probably the strongest one - is his Cologne address, typewritten translation of which I enclose, attached to a copy of Gilbert's daily press service, which contains some interesting translations. A third weakness of Schacht's, which I believe will disappear since our visit, is a tendency to run the Reichsbank according to the letter of the Bank Law as to the General Board of Directors, rather than to use these foreign contacts for the purpose of building up confidence not only among the directors, but among those to whom they would naturally report at home. The Reichsbank Act gives very little power to these directors, who are regarded in some quarters as a species of eye wash, to satisfy French and Belgian public opinion. I learn confidentially that at first he and Bruins, the Dutch Bank Commissioner, had some difficulties on this account, which have all been eliminated. The same has been true, possibly in matters of little importance, as to both McGarrah and Addis. Norman and I had a long talk about it, and, as Norman knows Dr. Schacht much better than I, Norman took it up with him, and, I guess, had a pretty plain talk. At any rate, when we met later, Schacht told me that Norman had given his hair a thorough combing and that he intended to follow his advice. I suspect that Norman originally sympathized with Schacht's position, but was persuaded somewhat by what I said to him. At any rate, Dr. Schacht tells me that if McGarrah and Addis give him an opportunity he will tell them every blessed thing there is to know about the Bank, and make it his business to convince them that he is striving to carry out the program in letter and in spirit.

Still a fourth weakness of Schacht's is possibly a little lack of sympathy between him and the Directorium, they being, as you know, the salaried, responsible staff of the Bank, which we might describe as Managing Directors. It seems that Schacht's selection was unanimously opposed in the Bank, and there are still some members of the directorium who resent an outsider coming in; and with them he does not get along as well as might be. But they tell me also that improvement has taken place in this matter.

And a fifth weakness, to be expected in a man of his character and temperament, is undoubtedly the fact that he runs his part of the show with an iron hand. He does it openly, frankly, and courageously, and seems to have the support of his Government, but it certainly would not do in America. And one needs somewhat to reconstruct ideas here in order to appraise the man, as well as the situation in the Bank. On the whole, I think it needed just that type man, and that he presents exactly the contrast with Havenstein which was necessary to accomplish the results that, so far, appear to be little less than a miracle.

This introduction, in a general way, will give you about all that I can say to his disadvantage. And there is so much to be said in his favor that I would need to go over much of the ground which we did ~~over~~ over a week in order to give you the many favorable impressions which I gained.

He seemed to be absolutely honest and frank, in fact, candor was the outstanding characteristic of all of our talks. He doesn't gloss things over; he seems actually to relish setting up and exposing the difficulties, and then attacking them with plans and projects for their treatment. No question that I asked him caused him to hesitate or display any evidence of reserve.

I went to Berlin with the impressions which we all have at home, that the Reichsbank was in a pretty comfortable position and the outlook fairly favorable. Dr. Schacht's first effort was to disillusion me; and produced the figures to show the facts of what the situation is, rather than permit me to carry away the opinion that everything was rosy. Much of the information he gave was volunteered. In fact he did not give us opportunity to try him out on many things, and his eagerness to have us gain the correct impression and understanding was perfectly obvious from the beginning.

Dr. Bruins and Shepard Morgan both say that that has been his attitude towards them. Those two, you realize, being the ones mainly charged with securing information about the Reichsbank, even more so than members of the General Board.

Now with this preliminary sketch of the man, I want to give you a word about the position of the Bank, as to its reserve, its credit policy, and what its immediate future must be.

The banknote issue today is about M.2,500,000,000 (leaving out the Renten marks, which must be separately dealt with). Against these notes the bank has a reserve of 58%, of which one-quarter is in divisen. In addition, it owns, or has at its command, in round figures, M.300,000,000 of divisen in the shape of invested assets abroad, which are not counted as reserve. Only bank balances and gold held abroad are considered as reserve. The drain on the bank's foreign exchange balances has been continuous since early in the year, partly caused, without question, by "payments in kind," which reduce supplies of divisen otherwise available; and partly by the payments under the British Recoveries Act. Were not these deliveries made without the equivalent cash payments in foreign currencies, the position of the foreign balances would be very different indeed.

Now it appears that the big reduction of over M.400,000,000 in the divisen balances abroad has been caused successively by various developments, each of which has shaken confidence in Germany's position. One was the failure to

withdraw the troops from Cologne; another the Hindenburg election (which is really no cause for alarm); another is the Stinnes affair; and still another, having nothing to do with politics, being the repayment of a loan of 5,000,000 Sterling made to the Reichsbank by the Bank of England, some eighteen months before it was really due.

Dr. Schacht maintains that if his reserve of divisens abroad should get below the 10% which he is allowed to carry in that form, it would be a shock to the credit of the Reichsbank, and to Germany generally, and that he cannot afford to have that happen. His margin, as you will see, is now getting rather narrow, as it is down to about \$75,000,000. The Government, in various forms, probably hasn't got over \$10,000,000 of available foreign balances left over from the old divisens office accounts.

Germany is facing some political reactions which cannot be escaped as the result of the negotiations for a "pact." I feel, and others here feel, that the agitation of the pact negotiations may, temporarily, create the impression abroad that the political situation in Europe is still most uncertain. They are also facing some disturbance to confidence abroad, which may result from the policy deliberately undertaken to force a liquidation as described below. When I say force it, I do not think any measures are needed beyond what are now in operation and the high cost of credit.

These developments may lead to withdrawals of short credits, placed principally in London and New York. They estimate that there are £25,000,000 credits in London, and, of course, we have a good many, though not as much as that, in New York. If any considerable part of these are withdrawn next month, when they expect the movement to begin, the invested divisens account may be entirely used up, the surplus reserves disappear, and the Reichsbank have great difficulty in maintaining its reserve. \$100,000,000 or thereabouts would wipe out the margin.

Dr. Schacht says that, rather than see the foreign value of his currency impaired, he intends, if it takes the last ounce of his strength, to continue to reduce the circulation so that the reserve will be maintained and the mark maintain its value; that is to say, he will meet demands for foreign payments by using his reserve, thereby maintaining the value of the mark. But, in order to use his reserve and yet not impair it, he must reduce the circulation. He states this frankly in public, and I gather from what I have learned of him, that he likely will do it, and that the most thoughtful people in Germany will support him in doing it.

Of course relief will be afforded by foreign loans, and these he will encourage provided they are well secured and are long in maturity.

In a word, therefore, he has from \$75,000,000 to \$100,000,000 of foreign reserves yet to be used before his reserves become impaired, and he must, therefore, restrict credit and, consequently, reduce note issues.

It is necessary, in order to understand the situation, to describe what he means by restricting credit. With us, it means "direct action;" with him it means something quite different. The Reichsbank has between 450 and 500 branches, which cover every part of Germany. Only 18% of their portfolio consists of private discounts for their depositors; the rest represents transactions with banks. No loans and bills, or other forms of credit, are given directly to industrial and commercial customers. Each branch has an absolute limit upon the amount of credit which it may extend. The managers, I believe, are instructed in a general way to maintain that position by using careful discrimination between loans for productive

and those for non-productive purposes. The Reichsbank contact is so intimate with all of the operations of German commerce and industry that this sort of rationing can be practiced through their system of branches, while it would be quite impossible in the United States. If, therefore, the reserves approach the danger point, he will simply reduce the amount of credit available at each branch. This will force a liquidation and bring notes into the bank, and thereby reduce his reserve requirements.

Assuming, therefore, that the crisis which he mentioned, will arrive in due course under present conditions, without the necessity of further credit restriction, it would seem to be unfortunate, and I think he would regard it as most unfortunate, if the pressure had to be increased simply because the reserves became impaired.

This stimulates his interest in long-time foreign loans, in the negotiation of the Gold Discount Bank paper, and has led him to ask me how I feel about the possibility of buying some mark bills. This was one of the last matters brought up in our talks. He explained very frankly that he had not the slightest intention of asking us for any credit. It was the last kind of thing that he wanted to do. But long-time credits would be helpful, and those he realized must be negotiated in the investment market. The discount of Gold Discount Bank paper would be helpful because it would furnish divisens, and would not be dangerous because exchange would be provided automatically to liquidate the discounts. The disposal of any mark paper, however, would impose upon them later the necessity of finding divisens to meet payment, and that he would seek to avoid and employ only as a last resort. He wanted rather an expression of my general sentiment on the subject, than he did anything in the nature of an answer.

I replied to him that it was a subject which would necessarily require consultation at home, and that I would be very glad indeed to write home about it, and, if possible, gain some expression of the views at the office.

I think in the long run that we should be prepared to do that business, but I was not yet ready to say that we could do it now, because of circumstances which I think I should outline to you quite frankly.

The first is that unless Germany and France can agree upon something in the nature of a pact along the line of the present discussion, the reaction from the failure would be unfavorable; that it might lead to a feeling that we were pouring money into a situation which was yet uncorrected, and simply postponing the day of ultimate political tranquility in Europe; and that our people might feel it was better to defer any action until more was known on that subject. It is possible that I gave him a more unfavorable impression on that score than is justified by the facts here, but I nevertheless do feel that there is room for great improvement in the situation as to the Eastern Frontier and the very uncomfortable relations now existing between Poland and Germany. It all relates to the "corridor," and Upper Silesia.

The next point was in regard to the pending crisis, which is undoubtedly coming, and which might also prove a jolt to foreign confidence, and I don't know how our people at home would feel about buying mark paper under those conditions.

The third point was the impossibility of determining whether these foreign credits were not, in point of fact, simply pouring money into a rat hole, which, through various devious channels, finds its way out ultimately through deliveries in kind, and likewise in debt payments to France and England.

The fourth, and by far the most important to us at the moment, was the serious criticism at home in certain quarters as the result of our having made a two year arrangement with the Bank of England, which was quite likely to result in some Congressional Inquiry this winter. I told him that I, personally, thought it would be unwise for us to add to the atmosphere of hostility in certain quarters by entering any long-time transaction on top of the one which has already been given such publicity; and that my general attitude would be that our own people would feel that we should not do so at the present time. I told him that if this subject came up before all doubts had been settled politically at home, the most that I could consider would be adopting a policy of maintaining a portfolio of mark bills in Berlin up to a certain amount. And if we ever did anything of that sort, certainly until this political question was disposed of, we could give no assurances of any kind that we would not require payment of the bills at maturity.

He seemed to feel that that might suit his book quite well, in order to take care of a seasonal situation such as they might have this fall.

I think his idea is that what with some foreign loans now being made, such as Berlin and Cologne, and some smaller ones; with the possibility of negotiating Gold Discount Paper; and a possible loan to the Rentenbank; he will be able to meet every possible demand for a long period, and until more favorable conditions develop, by having at his command somewhere from M.200,000,000 to ^{being} M.300,000,000 which he would only use in an emergency, and the last to be used the sale of mark bills in New York.

Norman was present when this conversation took place, and he has told Dr. Schacht that he would be very glad indeed to take up to £5,000,000 of mark paper, I believe giving him quite a long period in point of time; and afterwards he told Schacht privately that he would undertake to do so if Schacht needed that help. I think the idea was that if we were later at all interested we might buy some bills, the outside limit being, possibly, \$50,000,000. These bills would be prime paper, discounted with the Reichsbank, of a strictly commercial nature, bearing the name of drawer, acceptor and a bank indorser, as well as the indorsement of the Reichsbank.

After all of our discussions, and the intimate character of the information we gained from Schacht, I am convinced that the paper is just as good as gold. There isn't any possibility of the Reichsbank failing to meet such an obligation as things are now, or are ever likely to be, so far as the near future can be anticipated.

Of course if we should decide to do anything of that sort, it would be highly important not to have it a disturbing factor in our money market, so I stated definitely to Schacht that if we did buy mark bills from him, we would be unwilling to place the exchange at his disposal in New York, but would require him to take gold. In other words, he could, if he found his reserve becoming impaired, ship gold, say, to London, or elsewhere for the purpose of making the payments, and replace it in New York by selling us mark bills, and having us earmark gold for him, or even ship it, on his order, to other points. This would avoid putting our funds into the New York market. And as his undisclosed dollar reserves in New York are now all invested in one form or another, the use of those reserves if it had any effect at all upon the money market, would be in the direction of reducing loanable funds, rather than increasing them.

Dr. Schacht has promised to send me translations of the statements of the Reichsbank, the Rentenbank, and the Gold Discount Bank, and any other information that I want. If the situation develops pretty rapidly, - before I return home - he will come to London to talk it over again.

Now, as to my own impressions as to a policy, I can give you only a very brief outline, as it would take a volume to give you everything that I gathered in Berlin.

First, I believe that deliveries in kind are now draining Germany of potential reserves of foreign balances, the strain of which will gradually increase until within six months or possibly a year, it may be necessary for Gilbert to slow down. He realizes the position and is protecting himself by clauses in contracts, etc., in a very forehanded fashion, and my confidence in his wisdom in this matter is immensely strengthened by what he tells me of his care in anticipating developments.

Second, I believe that the tremendous confidence shown by Germany in the Dawes Plan as a means of relief, is something which must not in any event be shaken by attempts at modification, certainly for a year. The fat would then be in the fire, and, therefore, it may be the part of wisdom to ease things along, in reliance upon common sense prevailing in handling the matter.

Third, I believe that well secured credits to Germany (secured by mortgages on good properties) and not maturing too soon, are justified by conditions here.

Fourth, I believe that Germany intends to make every effort to earnestly carry out the Plan, but that most people are convinced that the full schedule of payments cannot possibly be maintained, and that some people are reluctant and unhappy in making these payments, but nevertheless see the wisdom of doing so. They are willing to do it, but cannot be glad to do it.

Fifth, I believe that short credits to Germany are a menace and should be discouraged.

Sixth, the general appearance of the country, so far as I have seen, and everything that people tell me, would indicate that Germany is ready to forge ahead as soon as they have been through the trial of a secondary period of liquidation.

Seventh, I believe that political developments in connection with the negotiation of the Pact, and the economic developments in connection with what they anticipate will be a business crisis, will injure Germany's credit abroad temporarily.

Eighth, I believe that during that period, which is likely to extend into the winter, help will be needed from abroad.

Ninth, The Bank of England is willing to let the Reichsbank have \$25,000,000, if help is needed.

And finally, tenth, we could probably afford to do so also, along the above general lines, dependent a little bit what happens politically both in Germany and with us in the course of the next few months.

Now, as Dr. Schacht has not asked us for any credit, but simply that I

Spa, 7.20.25

consider his position and the possibility that some day he may need one, all that I want you to do is to study this over, describe the situation to some of our directors who will be interested, especially Mr. Young, and then cable me as soon as you can what, in a general way, the reaction is.

I must ask you to use your discretion in discussing or consulting with the Washington folks. Of course they must know about a matter of this sort, but I do dread these recurrent leaks there.

Won't you pardon such a long letter, I could hardly give you even a rough impression without inflicting you with one.

Sincerely yours,

Ben. Strong

Pierre Jay, Esq.,
Chairman, Federal Reserve Bank,
33 Liberty Street, New York.

P.S. (7.2.25)

On reading over the above, which is just as originally dictated, I find it may give you the impression that the discussion of the purchase of mark bills was a little more specific than was really the case. The talk was very general, and the amount was only gathered by implication from Dr. Schacht stating that he would like to have M.200,000,000 or M.300,000,000 to fall back upon in case of need. And as Norman is willing to let him have M.100,000,000 (that is 5,000,000 sterling), I gathered that somewhere between \$25,000,000 and \$50,000,000 would satisfy his outside requirement.

I made no mention of the possibility of the German Government specifically standing behind any such transaction. It did not seem wise to do so at the present juncture, and, of course, the whole political situation here, as well as the situation as to making foreign payments, is quite different from what it is in England.

On the whole, I would be inclined, in case Dr. Schacht approached us on the subject, to intimate to him that we would like to have something from his Government in the way of an assurance that no obstacle would be placed in the way of repayment; but even this would be no more than an expression of an approval of the transaction, for, after all, it is Gilbert and the Transfer Committee who would have the final say.

As you will gather from the above, developments in Germany, as well as in England this fall are going to be of great importance.

Dr. Schacht wants to see me later, and will come to London for the purpose. It leaves me a little uncertain as to my plans, but I shall stay here at Spa, certainly for another week, as Norman is very badly in need of a rest,

P.S. (7.21.25 continued)

and looks and feels wretchedly. And I have felt the need of it myself.

We may take a week at some seaside place, visiting Brussels in the meantime; then do Paris; and leave Amsterdam and Vissering until the last.

B.S.

MADE IN U.S.A.
BOND
WWEIBNITT

ack
gpc
8/17/25

FEDERAL RESERVE BANK
OF NEW YORK

Spa, Belgium,
July 21, 1925.

PERSONAL & CONFIDENTIAL

Dear Mr. Jay:

Since dictating my separate letter in regard to the Rentenbank negotiations with the City Bank, I have received the enclosed description relating to the revaluation procedure, as proposed by the law of July 15, relating to mortgage loans and priorities. This was prepared in the Reichsbank at my request, and is a digest, of course, and not a copy of the law itself. You will observe from it how complicated the position becomes.

In this connection it must be borne in mind that while a large amount of these farm mortgages may be held by private owners, probably a still greater amount is in the hands of credit institutions such as savings banks, etc.

The revival of 25% of the mortgage loans makes necessary the similar revival of 25% of the liabilities of such institutions. It becomes very difficult to accomplish this, and is, of course, the first step in the direction of the revaluation of other forms of debts and credits.

While Dr. Schacht was earnestly opposed to the whole scheme, and believed that it would work considerable injustice to various classes, he, nevertheless, saw no escape from the plan because of the serious losses of people of the poorer and middle classes, some of whom are directly or indirectly a charge upon the State, or the industrial establishments of Germany, such as the railroad lines.

The best estimate that he could give me of the amount involved was M.40,000,000,000 for private mortgage debts, meaning that M.10,000,000,000 will be revived; and that the revival of the Government debt, at the rate of 5% for the portion which had been permanently held since July 1, 1920, and at the rate of 2-1/2% to holders subsequent to that date, will amount to around M.4,000,000,000 or a little more. In other words, the effect of the revaluation act is to bring into ~~existence~~ about M.14,000,000,000 of debts, - placing a burden upon one class of people for the benefit of another class.

It will be interesting to see how it works.

Sincerely yours,

Reu. Strong

Pierre Jay, Esq.,
Chairman, Federal Reserve Bank,
33 Liberty Street, New York.

About revalued mortgages - priority.

(Law of 15th July 1925)

According to the law voted by the Reichstag (third reading) on 15th July 1925, about revaluation of mortgages and other claims (revaluation-law) mortgages are to be revalued at 25 percent of the amount in goldmark. The so revalued mortgages maintain on principle their character as first or second etc. class securities. Any mortgages registered during the time from 14th February 1924 (the date on which the third emergency-decree on taxes, "Steuernotverordnung", went into force) to 1st October 1924 are preceded by right of priority by the revalued mortgages only up to the amount which is fixed by the said third emergency-decree on taxes, consequently up to 15 percent of the amount in goldmark. The remaining revaluation of 10 percent takes place behind the mortgages registered within the above mentioned period. Any mortgages registered after 1st October 1924 are preceded by the revalued mortgage to the full amount of 25 percent of the peace-value.

Special regulations are applied to this system. In the case of general revaluation to 25 percent such old mortgages as appear in the rear after the ~~first~~ first mortgages would obtain a position which would confer on them better right than those at the time of their rights origin. Since there presents itself a ~~press~~ necessity for obtaining credit both for agricultural owners as for owners of houseproperty, which is more difficult to attend to, ^{since} the more old mortgages enjoy priority before newly proposed mortgages, it appeared advisable to have recourse to such a way of settling rights of priority, in which maintenance of the principle that revalued right maintains its rank unimpaired, leaving to the owner a mortgageable place for

new mortgage-credit and which at the same time does not impair and prejudice the right and position of the mortgage-creditor as such right and position were at the origin. The new re-valuation law therefore conveys to the owner the faculty to have attached a marginal note, in order to secure a later registration of a mortgage (reserving the right to priority) to the amount of 25 percent of the goldmark amount of the re-valued claim; jointly with the usual rate of interest, which rights take place after the revalued claims registered as first priority and beforehand of the rights having rank after them.

Whenever the goldmark amount of a mortgage revalued and having rank after the first following mortgage (for instance 2^d or 3rd mortgage) is fully within the security-limit established by law for wards-funds (66 2/3 of the real estate value) then the owner is entitled to provide for a rank-reservation as well after this right and before the following rights up to the amount of 25 percent of the goldmark value of the revalued claim jointly with the usual rate of interest.

The aforestanding system is shown by the following example:

Revalued "national defence contribution" (II. art. II, § 3, paragraph 2, number 1 of the 2 emergency-decree on taxes of 19th december 1923 RGBl. I page 1205): this must, so far as the wards-security is to be appreciated as to relation of right to real estate value, always be taken as real estate value - 100 000 M, charge in peace-time 10 000 + 40 000 + 10 000 mortgages. These 3 mortgages are to be revalued to 2500, 10 000 and 2500 M. Since all 3 mortgages are within the peace limit for wards-security (66 2/3 percent), there will be behind each of them, by operation of the rank-reservation, an equal credit-
The registration of this rank -

rank-reservation on the "ground-book" jointly with registration of the revaluation, is compulsory. In case the value of the real estate is today but half of what had been stated at the readjustment of the "national defence contribution", then even today the third mortgage-creditor will be, if it comes to compulsory auction, in just as good a position as before, (irrespective of public charges).

The rank-reservation, registered for the owner, is of value only when the raising of the corresponding mortgage will be admitted at the present high rate of interest; for this reason has been added the stipulation, that it can be registered at the "usual" rate of interest. The possibility to admit a new mortgage to the free credit-spaces disappears of course to the extent these spaces have been filled by raising stable-valued, foreign or debts in Reichsmark. The aforestanding example goes to show that all the credit-spaces are filled in the case of an owner who has obtained, at the close of 1923, a stablevalued mortgage of 15 000 Goldmark.

Another special regulation has been made for such mortgages as have repaid during the time from 15th June 1922 to 14th February 1924; even in the cases where the creditor has without reservation accepted payment. Such mortgages may, although they are already cancelled in the "ground-book", be again registered on their old places of rank to the rate of revaluation, so far as the stipulations concerning public faith attached to the "ground-book", do not oppose ^{themselves} v. e. if no one else has given a mortgage bond fide on the real estate. Where such a case presents itself, the mortgage registered in the meanwhile takes precedence before the revalued mortgage to be registered.

The legal situation may therefore be stated as follows:

All papermark mortgages are to be revalued up to 25 percent of their goldmark amount; all of them maintaining their old places of rank. All mortgages, existing at the date this law takes force, of stablevalued or of foreign currency or Reichsmark will take, on solicitation, place on the credit-spaces held free through the "rank-reservation", in the order as they rank.- New mortgages made out after this law has taken force dispose of the "credit-spaces", free on the strength of the "rank-reservation", according to the free decision of the owner of the real estate. In case these spaces are filled, the new mortgages, of course, take rank behind revalued mortgages and behind rank-reservations. There is besides the possibility to register again such cancelled mortgages as have been repaid during the time from 15th June 1922 to 14th February 1924.

All public charges, by virtue of the law on charges on the industries, to 15.7 percent and by virtue of the Rentenbank-law to 5 percent of the "national defence tax", have of course priority before all other rights and remain untouched by the present draft of law.

A BANK MEETING

Governor Norman has held in mind continuously since the Genoa Conference that he is under obligation to have some sort of bank meeting, at which would be present various representatives of banks of issue, the object being to discuss the gold policy. His original expectation was to have a very informal, unofficial meeting, attended by Dr. Schacht, Dr. Vissering, Mr. Moll, himself and myself. This would be representative of those banks which are, to a greater or less extent on a distinct gold basis.

It seems that he has also been approached by both Robineau and Hautain to call a meeting. They suggested the desirability of having the banks of Italy, France and Belgium discuss the future of the gold standard, etc.

To the latter request he replied that he felt no such meeting would be profitable unless it were accompanied by friendly cooperation and political harmony. Hautain replied that while friendly cooperation might be possible, he thought that from some of those invited to the meeting political harmony could hardly be expected. After a talk with Dr. Schacht and me, Governor Norman decided that a meeting of that character was inadvisable, and I believe he has notified those three bankers.

When it came to discussing the other meeting, it seems that Governor Norman felt that the call for the meeting must necessarily be based upon the Genoa resolution, and that no meeting would be profitable unless there was a definite objective set out in the call. I told him that I did not care to attend a meeting, especially if some publicity could not be avoided, which had for its foundation the resolutions of the Genoa Conference; that such a meeting might be entirely wise from their standpoint; but I felt unwise from mine; and that the same, or even more satisfactory, objectives could be obtained by meeting these men individually and separately.

There is a certain amount of friction already between some of them, and a meeting of these five men, possibly with a representative of the Suisse

National Bank also present, would result in a very reserved discussion of affairs, and my own part in it would have to be that of an onlooker entirely.

So we decided not to have any such meeting, but to arrange separately to see Vissering and Moll, and probably Dr. Schacht again before leaving for home.

Of course the important thing is the subject to be discussed, which would be:

The Gold Policy. Governor Norman has come forward with a rather novel idea that the whole future of the credit situation depends upon the adoption of some policy by which the inflationary effect of the new gold production can be neutralized, and the gold so distributed as to do the least harm.

My own idea is quite the reverse of that. I think the movement of gold is the result of other factors which are capable of a certain amount of regulation or control, and that the flow of gold must be reasonably automatic in response to exchange conditions, and that, therefore, what we are dealing with is not the reserves of the central banks, but rather their credit policies, which are bound to have a strong influence upon the exchanges, especially to the extent that credit policies develop the employment of foreign portfolios.

The curious thing about Norman's position is that when he was in New York, the whole course of his discussion with us was directed against a possible heavy drain upon the reserves of the Bank of England. Since the resumption, however, gold has been pouring in on them at a rate which he considers rather alarming, and he is now worried about the accumulation of gold rather than its loss. The same thing, in a way, seems to have been true in Germany. The gold which has been accumulating has come partly from Russia, partly from South Africa, and the balance from Holland and Switzerland.

One of the difficult things to be dealt with grows out of the gold exchange standard development, which is so largely taking the place of the operation of a true gold standard. It seems that the new gold coming into the hands of the banks of issue is going to those countries which are on a gold basis,

The Gold Policy (continued)

where habit and the desire to make earnings is leading to its being employed rather than being earmarked. Very large balances are being so used in London, and is one reason for the ^{ca} dirth of bills in the market.

Governor Norman's idea has seemed to be in some way to force the direction in which this gold shall move. I, frankly, do not see how that can be done. The situation in each country is different. In Sweden, by various devices, they are resisting further acquisitions of gold. The Reichsbank has purchased all the gold which it can now afford to own without reducing its reserves of divisens. The Suisse bank had a surplus, which it is giving up. The same is true of De Nederlandsche Bank. The two last named seem to command a larger volume of foreign exchange than the two former. Our own position at the moment seems to be fairly stabilized. While the Indian demand has been somewhat reduced, occassionally they are still taking some gold, and enough to prove a great relief to Norman.

Now the inconsistency in the situation, to me, seems to be this: Here are these four banks of issue, operating in a part of the world where there is a distinct shortage of credit, two of which are in the position (according to their notion) of having gold forced upon them which they do not want, and fearing a period of inflation resulting from it. And both of them believing that their own future depends upon establishing lower prices for what they produce and consume, especially what they produce for export.

The probability is that the situation will be met by just what will develop from the present high cost of credit, namely, some business recession, some unemployment beyond what at present exists, a readjustment of wages, especially in Germany, and then a period of recovery of business based upon a lower wage and price level. I gather that the officers of the German Government are expecting some such development and look upon it with reasonable tranquility, provided it does not go too far. Stresseman did say that he looked to see some little social disorder this fall and winter, but that it would not be of very long duration, nor very serious.

GENERAL ECONOMIC CONDITIONS
IN GERMANY.

There seem to be certain inconsistencies in the reports which are hard to reconcile, but the following are my impressions from long talks with a good many people:

In the first place, the whole machinery is over-burdened still with the remnants of the organization which grew out of the inflation period. There are too many employes on Government payroll, and on those of private enterprises. The pension system is extravagant. There has been a vast mushroom growth of enterprises of light financial responsibility, mostly handling the middle stages of distribution of goods, which all agree must be eliminated in order that production and distribution can be brought down to economical bases.

Nevertheless, there is a great shortage of banking credit. Extravagant and wasteful expenditure seems to^{be} widespread still because of the habits acquired during the inflation period, and because of still some distrust of the paper mark.

The German Government is criticized by some of the people connected with the Dawes Organization for unnecessary expenditures; and Dr. Schacht himself is unsparing in his own criticism of some of the work that is being done by the Government. He says there is too much road building and road repairing. Housing projects have not yet been wholly discontinued. One example is the project which had been started before the war, and continued during the inflation period, to put all telephone and telegraph lines underground. They had an immense scheme calling for an expenditure of some M.13,000,000,000. Some of that work is still going on, and Schacht thinks it should be all discontinued. He says altogether too much money is being spent for extravagant food; that a few months of real business recession and unemployment will be helpful.

Von Siemens told me that with 70% of their pre-war output in his enterprise, they still have as many men on the payroll as before the war. But

that they could use 3,000 more men in his works around Berlin if he could find accommodations for them. The trouble does not lie with the artisan himself.

The product from the bench of the actual workman is quite up to pre-war standard, but the whole organization for bookkeeping, selling, etc., is badly overmanned. The same seems to be true throughout Germany from all accounts.

While there is a middle class of people who have suffered a good deal of distress due to the wiping out of their savings, the impression I gained is that standards of living on the whole have risen too fast and too high, and that they must come down.

One of the men who was in our Liberty Loan Organization, Schumann, stated that they had just imported 90 Buick cars, which had sold before their arrival, and that he believed a very large number could be sold. He was making plans here for the development of some sort of instalment plan sale of cars, and thought that large numbers could be imported. Dr. Schacht says that cars of that class are being imported into Germany, but they are offset by the export of more expensive cars manufactured in Germany, for which they have a good market abroad. That still does not seem to justify going into a large program for importing foreign manufactured cars.

Another difficult situation seems to be developing out of the deliveries of coal. We are now experiencing a period of depression in the coal business at home. They are having a serious time in England. Whereas the mines in Germany are pouring out coal at a tremendous rate, - two-thirds going to France. Coal is piling up in England and France and Germany. It looks as though competition of oil and electricity had considerably affected the steam coal business; that the industrial setback had also had a bad effect; but that France was willing to take all the coal she could get, believing that anything she gets in the way of reparation payments is better than nothing. The result may be a world-wide readjustment of coal prices, unless there are strikes in America and England, as now seems possible, in which event the shut down of American

REPARATION PAYMENTS

I have had a good many talks with Gilbert and Shepard Morgan about the course of the reparation scheme. So far, they seem to be well satisfied with what has taken place, but both feel a good deal of reserve about the future. Gilbert, for instance, is insisting upon certain reservations in all contracts for deliveries in kind, which will enable him at any time to discontinue making payments in Germany in marks, and requiring the French contractors for the goods to pay cash, giving him, thereby, a certain amount of foreign exchange.

I believe he has a similar reservation as to the British Recoveries Act Payments. And when the accounts were checked up,^{and} it was found that the British had been paid at a rate exceeding the rate at which the French had been paid, he actually required a repayment to be made by the British, which annoyed them quite a bit, but I gather, nevertheless, had the effect of creating a wholesome respect for Gilbert all the way 'round the table.

Gilbert and Morgan both express doubt as to whether the deliveries in kind can continue according to the schedule under the Plan without such a serious strain upon the reserves of the Reichsbank as to require modification before the maximum normal payments begin. He sees quite clearly that excessive payments reduce supplies of foreign exchange, thereby throwing a strain upon the Reichsbank to furnish the means of making foreign payments for the benefit of German industry and commerce, which in turn, as described in another place, has the effect either of forcing an impairment of the Reichsbank's reserves, or a contraction of its note issue.

One interesting thing in connection with all of this situation, each part of which is interdependent upon all the other parts, is the very high type of organization charged with administering the Dawes Plan, - men like Gilbert, Sterrett, Morgan, McGarrah, Addis, Bruins, McFadyen, Lerverve, in fact all of them with whom I have come in contact appear to be men of the highest quality of ability and integrity. And the same is reported to be the case with almost all of the

Spa, Belgium

FEDERAL RESERVE BANK OF NEW YORK.....7.22.25 - Reparation Payments, Cont'd

(2)

others. They seem to be working together well, and working well with Dr. Schacht, with the exceptions which I noted in a letter to Mr. Jay. And this presents a hopeful outlook for the future.

GERMANY'S ATTITUDE TOWARD SUPERVISION

There is one very admirable thing which stands out in discussions with Germans in responsible positions.

I am quite sure that if an American were obliged to submit to the interference and inquiries and controls which are now imposed upon Germany, the irritation to feelings, and the sense of subordination to control would be a menace to anything like tranquil conditions.

The extensive character of these controls in Germany is really unbelievable. A large part of the western frontier is in possession of a foreign army, extending right into the vitals of German industrial districts; foreign directors in the Reichsbank; a commissioner for supervising their note issue and accounts; and the entire railroad system in the hands of a French commissioner; all of the industrial establishments mortgaged to foreign nations, and in general under the supervision of a foreigner; government financing, the budget, and the whole scheme of central banking and foreign finance subject more or less to inquisitorial supervision by the Transfer Committee; they are called upon to make endless reports and statistics; to have matters of policy and specific transactions questioned; and yet, I must say that they seem to take it in pretty good spirit, and while, now and then, they may groan in private among themselves, they do come up cheerfully, so far as I have observed, and toe the mark. That also is a good sign.

POLITICS IN GERMANY

I have already described the favorable impression made by Hindenburg. He seems to be universally well regarded. Of course he is a very old man, I believe now 78, but his reputation is that of a rather kind hearted man of the highest rectitude, who has abandoned militaristic notions in the belief that he can aid in Germany's recovery under the present regime.

Dr. Luther is undoubtedly the strong man in Germany, and many people say that he is the strongest chancellor they have had since Bismarck. I met him three times, once at luncheon at Dr. Schacht's, once at luncheon at his own official residence, and again at dinner at the Gilberts. I had a long talk with him each time. And I must say he impressed me as straightforward, and a man of truly dynamic force. He is very outspoken, and seems to be absolutely independent in his views. He is known as a man without a party, and presents the anomaly of being the Chancellor but not a member of the Reichstag, as is the case of four other members of the Government.

Stressemann, of course, is a party man, who is not very well regarded, and is believed to be rather shifty.

A number of members of the cabinet were formerly Bureau Chiefs in the various departments, as there was a good deal of trouble in forming a Government after Hindenburg's election, and they had to take what they could get, putting the bulk of the strain on Dr. Luther. But he looked to me like a man of exceptionally sound constitution, and gave no evidence whatever of being under any strain. He is good natured, speaks rapidly and positively, and when he does not understand a statement in English very well, he instantly stops you and asks to have it explained. However he speaks and understands English well enough to get along very well. I understand that he has learned it within the last year.

There seems to be much satisfaction on every hand at the poor showing made by Ludendorff in the election. I think he got in the neighborhood of 200,000

votes. There is also a definite feeling that it was the vote of the women which saved ^{Germany} from socialism, or communism, or worse. Apparently the women are rather strongly nationalistic. They all tell me that the chauvanistic spirit has largely died out. Germany, except for the more extreme imperialists, is today ready, without hesitation to enter into definite obligations as to the western frontier and the permanent ownership of Alsace Lorraine by the French, and of Malmedy by the Belgians.

They definitely want four principal things:

(1) The rectification of the frontier with Poland; especially to do away with the "Corridor" which cuts Germany in two, and makes East Prussia a very difficult and expensive unit.

(2) The recovery of Upper Silesia. They say the coal mines are being ruined and that the Poles will never be able to manage the country. They greatly resent its assignment to Poland in the face of what they claim was an adverse vote by the population.

As to these two matters, they are willing to enter into definite engagements only to effect a rearrangement by negotiation, without resort to arms or military measure of any kind, and under reasonable supervision by the Powers, or by the League of Nations.

(3) Then they want to be free ultimately to bring about the incorporation of Austria in the German Republic. And to that, I believe, there isn't much objection on any hand.

(4) Finally, they want the immediate evacuation of the Cologne Area, which was due some months ago under the terms of the treaty; also of the Ruhr and of the sanction area, which includes Dusseldorf, Duisberg, and Rhurort. And they have hopes that the progress of evacuation will enable the second area, at Coblenz, to be evacuated before the end of the second five year period.

These matters are today the great outstanding subjects with the German Government and people.

As to internal politics, there seems no doubt that the Luther Government is developing a sense of security and tranquility which had not been achieved by any previous government. It appears to be a typical case of the strong and wise man, wise enough, in fact, to avoid attempting the theoretically perfect, by being willing to make reasonable concessions to public opinion, such as he has found it necessary to do in connection with the scheme of revalorization of debts, which, in principle, I believe he opposed.

I suppose the test of the strength of this government will come when some possible criticism arises from the negotiation of the pact coincident with a period of some unemployment and uneasiness about economic matters, which is likely to arise this fall and winter.

I was glad to find Dr. Luther most enthusiastic about the work which Gilbert is doing; and Gilbert, apparently, with a very fine feeling of respect and confidence in Dr. Luther. I think they all realize that the future of Germany rests very largely upon the wisdom with which decisions are made by the Transfer Committee. And Gilbert's behavior, the wisdom of the decisions made, and the force with which they are made, together with the character of his recent report, have put him in an almost unassailable position. There are, of course, complaints back and forth about various things, but, in the end, he seems to have his way, and yet keep them happy and satisfied.

Before visiting Germany, I had occasionally been bothered by what appeared to be a contradiction between what we were privately told, that Germany was sparing no effort to observe the terms of the treaty of Versailles, the various conventions, the Dawes Plan, etc., which reports seemed almost universally to be satisfactory, and, on the other hand, the official correspondence occasionally published which gave the impression that Germany was seeking by subterfuge and otherwise to escape the obligations imposed upon her. The occasion for this became rather clear when talking with the Germans themselves.

Privately they have a theory of their future which is quite different

from that which they exhibit officially, the explanation being that Germany probably desires now to live in peace, to have good relations with neighbors, to develop industrially, and to repay and build up what she can. But, officially, all contacts with neighbors, such as France and Poland and Belgium, are characterized by distrust. I think possibly the worst feature of the European situation today is the distrust which politicians have of each other. What they say privately, they feel unable to say officially. This lack of frankness will in time either bring the political organizations into conflict with the Dawes Organization or may have some influence upon the independent attitude of the Dawes Organization. But the encouraging offset to this situation lies in the very high character of the men who are administering the Dawes Plan.

Having had opportunity now to talk with such men as Luther, Stressemann, Schacht and some other members of the German Government, also Houghton, Dr. Schurman, Lord D'Albernon, the Belgian Ambassador, and the men in the Dawes Organization, I can see that this background of distrust exists everywhere. One consequence of this atmosphere is that the American and British Ambassadors seem to be constantly drawn into consultation for advice. Their attitude is to compose differences and bring about agreements.

Right now the French seem to be doing their best to continue negotiations in regard to the frontiers by correspondence, while the Germans are anxious to have a conference. The Germans believe that no settlement can be arranged by correspondence, and that the French insistence upon correspondence is for the purpose of defeating an arrangement; whereas the French are reported to feel that once they have a conference with the Germans, pressure upon them will be strong enough to lead them to make concessions which they are unwilling to make. It was interesting to me to note that Mr. Houghton, Lord D'Albernon, all of the German Officials with whom I talked, as well as Dr. Schurman insisted that a conference was absolutely necessary.

Dr. Schurman has suggested a meeting of no more than three men, without a big staff, and in a very informal way. And at least negotiations

Spa, Belgium

FEDERAL RESERVE BANK OF NEW YORK 7.24.25 - Politics in Germany, Cont'd

(5)

have progressed to a point now where they are considering where the meeting will be held. The British prefer London, but are willing, I believe, to go to Ostend. At least all with whom I talked were hopeful of being able to have a conference, and that the results would be in the main satisfactory.

RECEIVED
BOARD
NEW YORK

ALLIED DEBTS

I had some very interesting discussions with a number of people in regard to this whole subject, although my own part was more listening to a variety of complaints and suggestions, some of which, however, it will be well for our Government to heed.

The first came from Mr. Houghton, entirely unsolicited from me, being the result of some inquiries that Mr. Phillips made about the progress of the negotiations with the other debtor nations. Mr. Phillips, our Ambassador at The Hague, was just returning home to be present during the negotiations with the Belgians.

Mr. Houghton remarked that he was satisfied, as the result of his study of conditions in Germany, and of what he had learned in England since taking up his post there, that our Government was heading towards a dangerous situation if they insisted upon refunding arrangements with the French, Italians and Belgians, and were unwilling to suggest any modification of the British arrangement. He said the British would never suggest it officially, but would always resent the severe treatment imposed upon them if much more liberal terms were granted the others. But he felt even stronger that the rate of payment of debts to the American Government was liable to reach the point likely to cause serious disturbance in the United States to the exchanges and to stable banking conditions.

He asked me whether I thought our Government could be induced to volunteer a rearrangement of the British treatment. Mr. Phillips, as I recall, stated his belief that even if our Government were willing to do so, the Congress would never ratify such an arrangement, believing it to be unpopular throughout the country. I asked Mr. Houghton if he did not think that a very good chance still existed for doing that if refunding arrangements could be concluded with the other nations, and then submitted, together with a proposal for modification of the British plan. Mr. Houghton, who is an old member of Congress, said that he was

absolutely convinced that Congress would agree to it. He thought the difficulty was largely in the Funding Commission, - just as I do. He stated that Mr. Kellogg had gone home convinced of the need for some such arrangement.

He also asked me what I thought of the attitude of our Department in regard to loans, both Government and private, to countries which had so far declined to fund their debts, and I told him that I thought it was going to prove a serious mistake for the Department to exercise pressure in the way it had. It constituted each banking firm which had a loan declined the spokesman of the Department in explaining the reason for declining. Misrepresentations will be bound to be made and cause bad blood. Also, when loans were approved, notwithstanding the conservative formula of the Department, these bankers would be the instruments through which the impression would gradually be conveyed that the United States Government in some way was behind these foreign loans. I think, in fact, that that impression has already arisen in some quarters.

Mr. Houghton seemed to be troubled on that point himself, and I thought agreed with my suggestion that the way to handle these matters would be to give merely an acknowledgment to the bankers who reported proposed loans, and then, if there were objection, state the objection to the diplomatic representative of the foreign government concerned, and at once advise the banking firm that the Government had objected by that method and preferred that the loan be not made.

I told Mr. Houghton I thought the situation justified his making some sort of a report home, which I hope he will do.

He said that if our Government volunteered some debt readjustment with the British, it would have such a wholesome effect abroad that we would gain much more in prestige than we would lose in money.

When I reached Berlin, Gilbert told me very confidentially of his own correspondence with the Department when they attempted to require the New

part of
York bankers to apply/the proceeds of the loans to the City of Berlin and the City of Cologne to effect the transfer of some M.15,000,000, being our share of the reparation payments, for which no provision for transfer had been arranged. It seems that the Department cabled Gilbert two or three times asking his consent to the arrangement, which Gilbert positively declined, and finally sent a rather peremptory cable indicating that his previous cables had expressed his opinion and concluded the correspondence. I know he felt that the suggestion was at least unethical, - as I do myself.

Gilbert feels a good deal as I do about the pressure now being exerted through these foreign loans being offered in America. He told me that Janssen, the Belgian Finance Minister (who is a friend of mine) had been advised through the Belgian Foreign Minister of the receipt of a very peremptory note from our Department of State, which was almost a command for Janssen to come to Washington by a certain date named to discuss debts. It seemed that Janssen had only been in office a week, and had to prepare the budget within two weeks, making it quite impossible for him to leave Belgium. And he and the other members of the Belgian Government expressed the utmost resentment at the way in which the correspondence was conducted. Of course this does not help the debt negotiations.

Then, when I spent an evening with Dr. Schurman, our Ambassador at Berlin, he and Mr. Hill of the Department of State, who is on a special mission there, tackled me right away about the transfer of the M.15,000,000 and this whole subject of loan negotiations in America and the control now being exercised. I think Mr. Hill rather favored the attempt to grab a part of the proceeds of the Berlin and Cologne loans, but Dr. Schurman agreed that the proceeding was rather unethical, and that it should not be handled in that way.

The fact is that our Government has been led to agree to the Paris settlement and division of reparation payments without any scheme being arranged whatever for transfers of our share. The French are being paid by deliveries in kind, and the British are being paid by the operation of the Recoveries Act.

The only suggestion for dealing with the matter that I could think of was to make special purchases of potash in Germany, to be paid for out of the mark balances, and then sell the potash in America for dollars to the fertilizer manufacturers. No question of competition could arise, as Germany is the sole source of supply. Other suggestions have been considered, like toy contracts, contracts for certain types of fabrics which we import from Germany, etc., but the potash one strikes me as the likeliest scheme of settlement. Another suggestion is that we buy property for a new embassy in Berlin, to which Gilbert would readily assent, but it looks to me as though we would accumulate about M.15,000,000 a year for the next few years and then find that there was considerable doubt as to whether the transfers could be effected anyway, unless some supplementary agreement to the Paris agreement can be negotiated.

10-10-10
ANALYST
U. H. G.

FEDERAL RESERVE BANK
OF NEW YORK

Spa, Belgium,
July 23, 1925.

Dear Mr. Case:

One object of my trip abroad was to gather impressions which I could bring home with me, but you know that impressions of that sort fail, and lose detail with time, so I have used the little spare time we have had in dictating a narrative much as I would talk it were I at home. It is very rough, and as yet incomplete, but it will furnish something of a background for the letters which I have already mailed to Mr. Jay and others while you were absent.

see letter 7/27/25

Tissue copies of the dictation so far, will be mailed from Brussels, where we arrive on Sunday. And I am writing to impress upon you that I do not think this should go outside of the Officers Council. I would like to have you show it confidentially to our directors, if they would be interested in reading it, impressing upon them, however, that it is confidential (as a good deal of the information contained in it was given to me quite privately, and it would be unfortunate and react badly upon me, if it became known that I had given it any general circulation).

It will be something of a disappointment to me not to get into Poland, Czecho Slovakia and Austria, but to make that trip would be trying during the very hot weather here, and would take a great deal more time than I could afford. Besides that it would have entirely knocked out our plan for a holiday, which I was anxious to spend with Norman.

We are planning to reach Paris, after a couple of days in Brussels, by about Wednesday, July 29; then spend a week or so at some seashore resort; after which Norman may return to London and I shall go back to Paris, where Dr. Stewart will join me; and from there, if time permits, I will run up to Berne (otherwise I may ask the Suisse to meet me in Paris in case they would be willing to make the trip). After that, I am planning to return to London and have a meeting with Vissering either there or in Amsterdam. This will carry us along to the end of August or into September, and by that time we are expecting developments to be disclosing a good deal both in Germany and in England. It is going to be arranged also to have a meeting with Moll. However, the most important matters in which we are interested just now are Berlin and London. And I hope to come home well supplied with information which will be supplemented by a good deal that Dr. Stewart will dig out, as he is working along rather separate lines.

Dr. Bruins, the Dutch Bank Commissioner, invited Stewart to stay with him at The Hague, and then visit De Nederlandsche Bank, so he left us at Berlin for that purpose, and will be in London by now.

I hope you all keep well at home. We are disappointed to learn of the return of very hot weather.

I do hope that you and Mrs. Case have returned from your holiday in first-rate shape.

Please give my best to all at the bank, and the same to yourself.

Sincerely yours,

Re: Hroag

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank,
33 Liberty Street, New York.

P.S. In an earlier letter concerning the narrative of my impressions, I suggested that I would indicate which parts were particularly confidential, but, on the whole, I think it is better that no use at all be made of any of it until I get home and have a chance to talk matters over.

Ro.

"Rates"

COPY

FEDERAL RESERVE BANK

OF NEW YORK

Spa, Belgium,
July 25, 1925.

Dear Mr. Jay:

This is to confirm cable #27, which reaches me to-day via London, and which you will observe has evidently been somewhat garbled:

"Strictly Confidential for Governor. Important New York banks hear from London that declining money rates there are agitating for question of reduction of bank rate. Also that substantial volume of American funds returning from London due to lower rates there. That considerable volume American deposits in London have been released to continent. Would appreciate your comments on foregoing. If you have not written me regarding Class A directorship, please send your suggestions as I should like to get nominating committee appointed before I leave August 4 for vacation."

and to confirm the cable which I am forwarding in reply today:

"No. 3 (test) Strictly Confidential for Jay
Replying to your No. 27

- One New York rumors result from general discussions in London following large gold receipts. Arrest of increase of short deposits in London seems desirable. Relending on continent if true is purely European matter.
- Two Important immediate consideration is relation of two bank rates. If we must increase to 4% within say three months, London must remain unchanged. If we anticipate continuing unchanged for that period London might immediately reduce.
- Three If you apprehend that stock speculation may at any time necessitate increase to 4% that would justify London remaining 5% and probably be best we make increase immediately as suggested by Owen D. Young possibly selling some securities.
- Four If however our situation justifies hope of safely maintaining present rate for three months London may reduce to 4 $\frac{1}{2}$ % at once.
- Five Reduction in London would tend to encourage trade while increase in New York would be to discourage speculation. Please telegraph fully and immediately (Bently code) care National Bank of Belgium, Brussels, to arrive Tuesday, which course you propose.
- Six At this distance Norman and I now favor alternative paragraph 3 if you apprehend as stated. Although Norman here we have had no communication with London but on receipt your reply he will return there if desirable and cable you developments direct.
- Seven McGarrah away and probably unable to see him. Meantime director matter is as we left it. Shall I submit question to McGarrah by wire."

I shall await further word from you, as requested, with the keenest interest.

Sincerely yours,

(Signed) Benj. Strong.

Pierre Jay, Esq.,
Chairman, Federal Reserve Bank of New York,
33 Liberty Street, New York.

ANSWERED
AUG 10 1925
J. H. C.

FEDERAL RESERVE BANK
OF NEW YORK

W. S. B.

MADE IN U.S.A.

Brussels, Belgium,
July 27, 1925.

Dear Mr. Case:

With this I am enclosing the copy of a memorandum in course of preparation covering impressions gathered by Mr. Strong. It is the one he promised to send.

[See earlier in file]

Also there is a copy of the translated Reichsbank statement, concerning which Mr. Strong wrote the other day.

At present he is hopeful of leaving for Paris on Wednesday, as he believes today and tomorrow will finish the discussions at the National Bank of Belgium. But something depends on the reply to his cable about rates.

Very truly yours,

M. S. B.

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank of New York,
33 Liberty Street, New York.

ANSWERED
(ack.)
AUG 10 1925
J. H. C.

WEEKLY STATEMENT OF THE REICHSBANK
JULY 7, 1925

ASSETS:

1.	Reichsbank shares, not yet issued.....	RM 177,212,000	
2.	Gold (bullion) as well as German and foreign coin, one pound (the pound equals 1/2 kilo) fine calculated 1392 RM, divided as follows:		
a.	Gold at Home.....	RM 974,947,000	
b.	Gold (not pledged) with foreign central banks....	RM 90,654,000	1,065,601,000
3.	Foreign valuta (Devisen) used as cover.....		355,200,000
4.	Portfolio of bills and cheques.....		1,579,680,000
5.	German coin.....		66,930,000
6.	Notes of other German Banks of issue (not including the Rentenbank).....		18,936,000
7.	Loans against securities.....		15,611,000
8.	Securities.....		201,344,000
9.	Sundry Assets.....		685,708,000

LIABILITIES:

1.	Capital		
a.	Issued and paid up.....	RM 122,788,000	
b.	Not yet issued.....		177,212,000
2.	Reserve funds		
a.	regular reserve funds, provided in the law.....		25,403,000
b.	special reserve fund for future dividend payments.....		33,404,000
c.	sundry reserve funds.....		127,000,000
3.	Outstanding Circulation.....		2,442,639,000
4.	Other Liabilities on call.....		573,984,000
5.	Liabilities on term.....		-----
6.	Debts toward the Rentenbank.....		2,142,000
7.	Sundry Liabilities.....		661,650,000
	Bills rediscounted	RM 540,406,000	

(Translated by the Reichsbank in Berlin, July 10, 1925, and sent to B.S. at Spa)

RECEIVED
AUG 7 1925
S. H. C.

FEDERAL RESERVE BANK
OF NEW YORK

Winston

48

*ack
J.H.C.
8/19/25 by letter*

ANSWERED
ack
AUG 13 1925
J. H. C.

Brussels, Belgium,
July 28, 1925.

CONFIDENTIAL:

Dear Mr. Case:

Before sailing, I told Mr. Winston that I would advise him if I learned anything of importance bearing upon the debt negotiations. And this will serve to inform you of discussions which we have had with Governor Hautain of the Banque Nationale de Belgique, which bore something upon that subject. A spare copy is enclosed for Mr. Winston's use. *Sent Winston Aug 7. JMG*

Of course you and he will understand that the communication is private and confidential, and to be used with much discretion.

It was carefully explained to Governor Hautain that my visit here was quite private and unofficial; that I desired to discuss especially monetary matters in which all banks of issue are interested; and any discussion of the debt incident to purely private and banking matters must be regarded as wholly personal, and not in any way representing official views.

It develops, as I hope will be disclosed by this letter, that the subject of the Belgian Government debt to our Government is intimately interwoven with the monetary position in Belgium; with the subject of the revaluation of the Belgian franc; with the future of the National Bank (whose charter expires in about three years); and, quite obviously, with the budgetary position of the Treasury.

It should first be understood that the gentlemen who are visiting Washington to negotiate a debt settlement, Messrs Teunis and Francke, with the Belgian Ambassador, Chevalier de Cartier, are all men of experience in banking and finance, but no one of them especially acquainted with the principles relating to monetary affairs and the operations of the national bank. The Minister of Finance, however, Monsieur Janssen, was for many years an active director in the Banque Nationale de Belgique. He is, himself, a lecturer on economics at the University of Louvain, and has an opinion in regard to these matters which is probably quite different from that of the average private banker. He has, however, been in office but a few weeks, and this, unfortunately, had the effect of preventing his visiting America with the mission, as he was in the midst of preparing the annual budget just at the time when the mission was called upon to sail.

The following observations are justified by my discussions with Monsieur Hautain:

1. Belgium intends to effect a settlement of the American debt if terms can be reached which they can reasonably feel are supportable, and will not prevent the stabilization of their currency.

2. Monsieur Hautain, probably with the sympathy of the Minister of Finance, is determined, if possible, to effect a devaluation of the franc and a re-
FRASER
of the currency position.

of hope of some special recovery from Germany on account of the so-called currency debt (which will be described later) and which hope, so far, has proved to be fruitless. Monetary reform has, therefore, been delayed because up to the present time the Treasury has been either unable or unwilling to balance the budget.

4. A further difficulty common to almost all of the countries in similar position, has been the adverse balance of payments, due partly to the need of large imports, and partly to the fact that citizens having investments abroad have been timid about the stability of the domestic currency, and, instead of bringing the income home for investment, they have invested it abroad.

And finally

5. The revaluation of the franc and monetary stability in Belgium will be impossible, according to Monsieur Hautain's view, with which I agree, if the burden of payments on the American debt is heavy, especially in the early years.

He tells me quite definitely that Monsieur Janssen will be able to balance the budget; that the Government stands ready to impose new taxes; but that the reorganization of the budget depends upon the outcome of the Washington negotiations. He also tells me that the budget deficit has been decreasing and that the adverse balance of payments due to the adverse trade balance has been steadily decreasing. And he believes that if a satisfactory funding arrangement can be effected, and the currency stabilized, there will be a considerable improvement due to the return of income, and very probably of capital which has left the country.

The technical position of the bank is most interesting, and bears directly upon the settlement of the debt.

The Germans, as you know, during the occupation of Belgium, imposed an issue of marks upon the Belgians, not through the National Bank, but through the Societe Generale, which was employed as the instrument for the emission of large quantities of paper money, at one time exceeding 7,000,000,000 francs. After the armistice, the National Bank retired the paper marks by issuing their own paper, the Belgian Government assuming the obligation of repayment to the Bank, and undertaking to negotiate some settlement with the Germans. The amount of the obligation of the Belgian Government to the National Bank on this account is now about 5,300,000,000 francs. The Belgian Government also owes the National Bank something over 400,000,000 francs, that debt having originated in war levies imposed upon the Belgians by the Germans. So that the Government debt to the National Bank on account of the German currency assumed by the Bank, and the German levies upon Belgium, amounts to 5,700,000,000 francs.

The note issue of the Bank is undoubtedly excessive for a country of the Belgian population, being, in fact, \$50. per capita. We estimate roughly that it is 40% or thereabouts in excess of what it should be. Probably a sound policy would necessitate reducing both the portfolio and the note issue of the bank before any method of devaluation is arrived at. But, unfortunately, the Bank's position is such that this can hardly be effected at the present time.

The Bank's portfolio, which nominally appears at 1,660,000,000 francs in its statement, is composed of the following items:

- | | | |
|----|------------------------------|--------------------|
| 1. | Commercial bills | Francs 540,000,000 |
| 2. | Lombard Loans | 230,000,000 |
| 3. | Portfolio of Foreign Bills | |
| | representing the invest- | |
| | ment of balances, principal- | |
| | ly in New York, acquired | |

by the Government as the	
result of the last two	
American loans	880,000,000

This 880,000,000 francs represents roughly \$44,000,000 at the rate of twenty francs to the dollar.

All the ^{Government} bills in the Bank's portfolio represent the debt of the Government to the Bank, above described, arising out of the German occupation.

With a domestic portfolio of only \$35,000,000 or \$40,000,000 it can be seen how slight is the power of the Bank to effect any shrinkage of the currency, except it is brought about by a retirement of the Government debt growing out of the German occupation; and Germany is paying nothing on account of its liquidation.

The task of the Bank, and of the Government, therefore, is to secure either some adjustment from Germany on the one hand, or effect some monetary transaction on the other hand without German aid, which will enable the Belgian Government to repay to the Bank a sufficient amount of this debt so that the Bank will be protected in some program of revaluation.

The reserve of the Bank against its note issue today, adding its domestic holdings of gold and its foreign balances in gold paying countries, amounts to something slightly over 30% of its note issue, - much too small a reserve for a country like Belgium, which depends so largely upon the outside world for supplies of food.

I think that Monsieur Hautain feels that if a funding arrangement is made with America involving any considerable payment at all at the present time, it would imperil the monetary position of the country because of the drain on its foreign reserves, which I confess would seem to me to be inevitable. That drain of course is liable to be all the greater in case the budget is not balanced. And I may best express his own views, which he has stated to us with the utmost frankness, by describing roughly a plan which he has in mind which contemplates concluding in one operation the funding of the debt to America, the balancing of the budget, the revaluation of the franc, the establishment of an adequate reserve for the Bank, and placing the bank in position to control the volume of the currency issue, and thereby maintain its international value.

If the funding arrangement with America is moderate in its demands for foreign payments, he would then propose that additional tax resources be found at once, which he says he believes could be done. The Parliament would then be asked to revalue the franc at roughly one-quarter its present gold value, leaving the present note issue in circulation, but, in fact, reducing the amount of gold in the franc to one-quarter, thereby enabling the bank to redeem, say, four notes of the present issue for one franc of old gold value. At the same time Parliament would be asked to extend the charter of the Bank. If this could be done, the Government should prepare at once to endeavor to float a long-time loan, probably in America, but preferably with British, Dutch and Suisse participation, to a total of \$150,000,000, the entire proceeds of which would be applied by the Belgian Government to repaying an equivalent amount of the debt to the Bank. The figures, when worked out roughly, are as follows:

The conversion of the franc from its present	
gold value to one-quarter of its present gold	
value would at once enable the bank to increase	
the franc value of its gold reserve by 4 to 1,	
which would give the bank a nominal profit on its	
gold of	1,200,000,000

That is to say, that amount of gold would serve as reserve for four times the amount of currency.

This profit on the gold reserve would be applied to the reduction of the Government debt of 5,700,000,000 to 4,500,000,000

The proceeds of the loan of \$150,000,000 would furnish the equivalent of 3,000,000,000 francs of foreign currencies, and reduce the Government debt to 1,500,000,000

This addition to the reserve in foreign gold currencies to the present reserve would give the Bank a total reserve of nearly 65% against its note issue.

If the balance of payments continued adverse to Belgium and threatened the exchange position, it could be maintained by drawing on foreign balances which would be sold in the market in Belgium, and, of course, payment being made in Belgian currency, would automatically reduce the note issue, and have the effect of maintaining its international value.

The plan has many admirable features. It depends, obviously, upon the following very important factors:

1. A satisfactory debt settlement with America.
2. Success in placing a large loan in gold standard countries.
3. A balanced budget.
4. The reestablishment of a reasonably normal balance of payments, of which they feel fair assurance.
5. Legislation by Parliament authorizing the revaluation of the franc, and extending the Bank's charter.

I draw the conclusion from our conversations that, unfortunately, the Belgian Government, as the French, has been pursuing the myth of much larger payments by Germany than are within the bounds of possibility, and it has only been the adoption of the Dawes Plan which has moderated this view and brought the Government, as well as the Bank, face to face with the realities. Even now I find that they have some lingering hope that Belgium and Germany may find it possible to make some private arrangement, outside of the Dawes Plan, for the adjustment of the German debt arising out of the currency inflation.

The proposition which has been in Monsieur Hautain's mind, though unofficial and private, has been the possibility that Belgium might return the Province of Malmedy to Germany, the consideration being some adjustment of the debt by the Germans. Of course any such program might have the effect of scrapping the Dawes Plan, all of which was pointed out to them. And I, personally, feel that any proposal for changes in the western frontier just now, during the pendency of the pact negotiations, would arouse the bitterest opposition in France, just as would any plan to circumvent the Dawes Plan.

I explained to Monsieur Hautain that this, of course, was none of my business; that I was only interested in monetary matters. But I personally expressed the view that he was pursuing a will o'the wisp, and that it was better to face the possibilities now.

It seems that he discussed the proposal a week ago with Dr. Schacht and Mr. Gilbert. Schacht may have given him some encouragement; but Gilbert answered that he urgently hoped the question would not be raised, and I imagine left it at that.

For lack of time I am obliged to dictate this letter rather hurriedly from a very few notes, and without opportunity to draft it for correction.

My conclusions are roughly:

That there is a very honest desire in the minds of Governor Hautain, of the Bank, and of Janssen, the Minister of Finance, to settle the debt question, and with it to settle all of these monetary questions, and to put Belgium back squarely on a gold basis just as soon as possible.

That the advantages of an arrangement, somewhat as suggested in principle by Hautain, seem to be obvious, although, of course, it would require examination in more detail than I have had opportunity to give it. And it would especially require consideration from the standpoint of the market in America for another large loan to Belgium, which might, even with the participation of other countries, amount \$100,000,000, or even exceed it.

There are certain points which Monsieur Hautain fully appreciates, and emphasized strongly in his talk with us. One is that the restoration of the gold standard in Belgium will afford protection to the Bank against excessive currency issues because of budget deficits and Government borrowings, which all banks of issue in Europe just now dread. He also understands that there must be an intermediate period during which the gold exchange standard must be substituted for a true gold standard. But Monsieur Hautain believes ultimately in the return to monetary gold circulation, and to actual international gold payment, as before the war. He appreciates that the reestablishment of currencies throughout the world on the gold exchange standard presents the danger of credit inflation in gold standard countries because of the large accumulation of balances by the banks of issue, which they will be constantly tempted to employ in the money market, and because of the inevitable attraction of gold from the mines and from non-gold standard countries to the gold standard countries. He is, therefore, a strong advocate of the principle of cooperation between the banks of issue for the purpose of controlling the possibilities of inflation; and I gather that he would even be willing, in case his program could be carried through, to actually earmark gold to the amount necessary, rather than to put funds in the market, in order to observe practically, as well as in principle, an international policy of inflation avoidance.

There is one danger in Belgium which strikes me as possibly imminent if the currency situation is not gotten in hand. I have been amazed to find, contrary to my expectation, and to what I had heard at home, that prices in Belgium are far lower than they should be considering the per capita circulation. To illustrate: We are occupying rooms in the best hotel in Brussels, on the best side of the hotel. The rooms with bath cost from 45 to 50 francs a day, say \$2.35. An excellent dinner in the hotel, with wine (and not a cheap wine at that) costs about \$2.00 per person. Last night three of us dined in one of the most expensive cafes in Brussels, where prices are supposed to be high, and were high before the war. We had a bottle of vintage champagne and a very excellent dinner indeed, the cost being about \$2.60 each. Fixed prices of articles in the stores appear

ridiculously low compared either to English or American prices, and considerably lower than German prices, so far as I could gather.

If the National Bank of Belgium has no means with its present small portfolio to control the note issue except through retirement of the Government debt, and if the Government, being unable to collect from Germany, is, nevertheless, obliged to make heavy debt payments in America and unable to deal with its debt to the Bank (and thereby deprive the Bank, through the Government debt repayment, of the means of controlling the currency) I can see nothing in the future for Belgium except advanced prices. Why it has been so long deferred amazes me.

This year should be an excellent year to deal with the monetary problems providing the various factors enumerated can be satisfactorily dealt with, because by all appearances, not only in Belgium, but in all of Europe, it seems likely there will be an excellent crop, with the minimum requirement of foreign purchases. Belgium has always had to import a large amount of food, and the crop will be a relief in this respect.

I am, therefore, hopeful that when the funding commission comes to meet the Belgian commissioners, they will not overlook the importance to us, as well as to the rest of the world, that the progress of monetary restoration abroad, upon which our foreign trade depends so fundamentally, shall not be impeded by attempting terms which will make monetary reform difficult or impossible. We must not overlook the fact that the Dawes Plan affords protection automatically against an excess of foreign payments, and places a very skillful organization in charge of affairs in Germany to supervise foreign payments, so that the world may be convinced that the evidence of capacity limit is conclusive and not in any way falsified. A settlement such as we made with England affords no such protection to the monetary position, and sets up no organization of supervision. If the lines of the British settlement are followed with Belgium, they will simply be taking the risk, and we the consequences of failure.

I am sorry to have written such a long letter, which I would hope to have avoided had I the time to draft and correct it.

I should explain to you, as well as to Mr. Winston, that the information received from Monsieur Hautain was most confidential; that these plans have probably not been discussed beyond the walls of the Bank and of the Finance Ministry; and that they are not to be publicly disclosed, though they may be used discreetly in connection with the problem he is now dealing with.

Sincerely yours,

Benj. Strong

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank of New York,
33 Liberty Street, New York.

DISCUSSIONS WITH MONSIEUR HAUTAIN
BRUSSELS, JULY 27, 28, 29, 1925.

The Belgian Budget:

The Belgian Government, as the French, have had a normal budget and an extraordinary budget, the latter having to do with restoration work and having been predicated, more or less, upon the theory that in some way Germany would pay. Because of the size of the extraordinary expenditures, the Belgian budget has not balanced, and last year the deficit was something like 1,500,000,000 francs. But the extraordinary budget will be very much reduced this year, and Monsieur Hautain believes that Monsieur Janssen will be able to balance the budget unless the American debt payments are too heavy.

They assume that the funding arrangement will be made, and the commission undoubtedly went to America with an honest endeavor to effect a settlement, and probably with pretty broad authority to deal with the matter.

Monsieur Janssen, the Finance Minister, is an economist, who lectured at the University of Louvain for a good many years at the same time that he was a director and an active official of the National Bank. I have known him for a good many years, and have had the same favorable opinion of him that others generally hold. He is quite unlike the common type of Gaul; not at all excitable; very well posted; apparently a thoughtful, deliberate man of sound views, and the determination to do the right thing.

It is opportune that they should have a Minister of Finance who was educated in the National Bank, and who is thoroughly alive to the perils of an unbalanced budget to the monetary situation.

The Belgian citizens still have large investments abroad, which will ultimately be resources of great value over the reconstruction years.

The National Debt:

The present debt is between 40,000,000,000 and 45,000,000,000 francs (the amount, of course, being estimated because of the need for valuing the foreign obligations according to the international value from time to time of the Belgian franc). Of this total, the floating debt is 5,500,000,000 francs. There seems to have been no difficulty in keeping the floating debt rolling along. There has, however, been a deliberate effort to keep the bank rate down so as to avoid high rates of interest on the Government borrowings. It seems that the Bank is free in fixing its own discount rate and loaning rate on all classes of business except upon Government securities, which requires the approval of the Government before it can be changed.

Notwithstanding the heavy debt, Monsieur Hautain states that the amount discounted at the Bank is negligible, being only about 250,000,000 francs. The Government makes no effort to use the Bank, and will not do so. He justifies the low bank rate for the Government's benefit by stating that the Bank Rate is completely ineffective. The amount of their portfolio of discounts and loans is so small that a high Bank Rate would accomplish nothing, and the only way in which they could control is by rationing, just as has been done in Germany.

While the national debt is very heavy, he does not feel that it is beyond their capacity to take care of the service of the debt.

In general, business in Belgium has been pretty good, and the crop outlook is excellent. The only two questions which cause them serious disturbance are the funding of the American debt, for which they fear the burden will be too heavy, and the prospect of complete loss of the claim against Germany on account of the issue of marks. The Bank is protected by the Government's obligation, but, obviously, it would be much easier all around if this particular debt, which has a strong moral support, could have been given some priority in the Dawes Plan.

The German Debt:

This matter is described in my letter dated July 28, 1925 to Mr. Case.

It happened that I was in Belgium^{in 1919} when the conversion was being dealt with by the National Bank. The Government had a mistaken notion that it was their duty to their own citizens to take over this issue of marks at a very high rate of exchange. And they did it in a very clumsy fashion anyway. Instead of closing the frontiers to the importation of Belgian marks, they gave notice in advance and converted them at a high rate, - I think at the equivalent of 17 or 18 cents. The result was that a very large amount of this paper, which was not within Belgium at all (in fact was in Germany) at once flowed in in order to get the benefit of the conversion rate.

Twice the Belgian Government succeeded in negotiating an agreement for repayment of the debt by the Germans. The papers were actually signed, and then the Reichstag declined, in both cases, to ratify the agreement. The debt was recognized by the Treaty of Versailles, but when presented for preferential treatment at the time of the adoption of the Dawes Plan, the claim was rejected. And it looks to me as though whatever Belgium recovers will be through the percentage accruing to Belgium under the Dawes Plan; and the priority there will be cleaned up before long and Belgium will be left with this debt unliquidated entirely.

So the burden of repaying the Bank will fall entirely upon the Belgian Government, and, of course, if the Belgian franc should be revalued at, say, one-quarter of its present nominal value, and gold payment then be resumed, the main protection the Bank could obtain would be by some arrangement with the Belgian Government by which they will promptly repay to the Bank a large proportion of that debt. And the only way in which the Belgian Government can do that will be by borrowing in a gold standard country or countries. Hence the plan proposed by Monsieur Hautain.

Stabilization:

Notwithstanding the situation as to the so-called mark debt, Governor Hautain is determined to propose a plan to revalue the franc, always provided the burden of payments to America is not too heavy. This subject is pretty well covered in my letter to Mr. Case, dated July 28, 1925.

Monsieur Hautain admits that if his program can be carried out, it means a higher bank rate. He believes that the maintenance of the international value of the new franc can only be accomplished by a foreign loan which would furnish foreign exchange that the Bank could sell to the market, thereby reducing their circulation in just the same way that any reduction of the portfolio would effect a reduction in the circulation. This reduction in the circulation would have the effect of driving the banks to discount with the National Bank; and that, in turn, would make a high bank rate effective in controlling expansion.

Foreign Relations:

Monsieur Hautain states that in a small way the Belgians are gaining some interests in Russia and in a larger way in Poland. They have always had quite a little business with Russia and Poland, and they are now hoping to develop it by making some investments there, and particularly by furnishing management to their industries. He says that the developments in Poland have been very satisfactory and profitable. These are in connection with the textile and engineering industries. But he does not think their trade will be restored to what it should be until after confidence is again restored in the stability of the Belgian currency.

Foreign Financing:

I pointed out to Monsieur Hautain that a loan of \$150,000,000 was a large sum of money for a small country, especially following as it did the placing of other loans in America, and asked him if he had any plans.

He said that the fiscal agents of the Belgian Government were Messers Morgan and the Guaranty Trust Company. And he wanted to know how best to handle a new loan, - whether they should have a competition and invite other houses in, etc., etc. He said that not a week passed without their being approached by American bankers for some of that business.

I told him that I thought it was a mistake to shop around; that there were, of course, a number of good houses who could handle the business; and that they might be justified in employing them if their regular agents could not handle the business satisfactorily; but that it was a great mistake to make inquiries of various houses at the same time and so unsettle the market for their own securities.

I also told him that I thought their budget position would be a detriment in these negotiations, and he admitted that, stating that the budget should have been balanced before, but that it was always the myth of collections from Germany that stood in the way.

He was very insistent upon the need for separating the French from the Belgian franc. They move together now almost exactly. It was pointed out to him that the only way to do that was to revalue the Belgian currency, put the revalued unit squarely on a gold basis, which would stabilize it, and then the French franc would fluctuate independently.

Central Bank Cooperation:

Governor Norman and I had a long talk with him about this whole subject. He agreed that a general meeting was at present out of the question, but thought these private meetings would produce better results.

I doubt if he much understood the possible dangers resulting from the widespread adoption of the gold exchange standard. When this was discussed with him, he seemed to think his bank would gladly cooperate in any sound plan to eliminate that danger.

He expressed himself as being quite willing to go to London before I return home, and was rather anxious to have a meeting with Vissering present. For him he has a very high regard. They seem to be in close communication.

Relations with the Federal Reserve Bank:

The morning before I left, we had a couple of hours together alone. I explained to him in considerable detail the scheme by which the Federal Reserve System conducted its foreign business, the legal limitations upon what we could do, the arrangement for having one bank represent all twelve banks in the system. And I pointed out to him what the result of our relations with the Bank of England had been, giving him the impression, so far as I could, that we were ready to discuss such relations with him, but that we felt that that subject generally should await the developments of the funding negotiations in Washington, and possibly the result of any Congressional inquiry which might take place this winter.

He is very anxious to establish close relations with us as soon as we are willing to have him do so. He thinks it might be most helpful were he able to sell us some of his portfolio of bills, and I believe he would be ready at any moment to turn over all of his American business to us. I pointed out to him the unwisdom of doing this instantly, because of the antagonism it would create among our members, but that ultimately some such arrangement was what we should work to. I think he proposes to write us about it later. I think it is rather

Relations with the Federal Reserve Bank, continued:

important that we should gradually have the account turned over to us, as they may have very large American balances, and the importance of the relation to our money market is obvious. The National Bank must have \$50,000,000 abroad at the present time, possibly more. And if the revaluation scheme should go through it might be three or four times that amount.

Bankovni:

We had a little talk about this, although there was nothing special to be said. I explained to him our reasons for making the loan, and that we were glad to have him hold the gold for us; but what we wanted was to see the National Bank established and functioning normally as a national bank should; and that we would probably carry the loan along, suggesting to them now and then that progress should be made in that direction.

General Impressions:

My impressions from the visit with Monsieur Hautain were quite favorable, as were Governor Norman's.

I think possibly the only adverse comments would be, first the delay in balancing the budget, which probably was not justified, being based, as in the case of the French, upon the vain hope of German payments; second the proposal for a separate adjustment with Germany, outside of the Dawes Plan, involving the surrender of Malmedy against some scheme of payment. This plan struck both Norman and me as visionary and impossible, and involving a great variety of dangers and difficulties which the Belgians do not seem to fully comprehend.

On all other points, however, it struck us that Monsieur Hautain was sound; that his proposals were of the right kind; and that he was an honest advocate of sound finance and sound monetary conditions.

I have no doubt that the bank is in excellent condition, and that the clearing up of the Government finances will enable it to function normally.

*Walt
J.W.C.
J.W.C.*

Grand Hotel Britannique
Spa, Belgium
July 25, 1925.

My dear Dr. Stewart:

Enclosed are copies of cables so far exchanged regarding rates. You will observe some change of attitude since our discussion in Berlin. This arises partly from further reflection and discussion, but considerably because of intimations of a possible rate reduction in London, the consequence of which I fear might have a distinctly bullish reaction on our stock exchange.

Governor Norman and I are agreed that a runaway stock speculation in New York would be a distinct menace to the position on both sides, requiring, as it might, more vigorous rate treatment later than would be necessary if we were to begin now.

A letter received from Mr. Jay since you left indicates such considerable crop improvement that there is always the possibility of a bull stock market being followed by commodity speculation. Were we forced into a situation later in the year, and in the midst of the fall demand, where a 5% rate became necessary, London would then be required to go to 6% - a situation which by every means should be avoided, especially in the early stages of the gold standard resumption.

This letter will be delivered to you by Mr. Norman's friend, Mr. John Hugh Smith, who is also carrying a note to Sir Alan Anderson.

Please discuss the matter in a preliminary way with Sir Alan, as you will observe that Governor Norman is willing to go to London on Tuesday night if my cable from Mr. Jay indicates that his presence is desirable, and if Sir Alan desires to consult before settling this question.

If Governor Norman does go to London, it will be with the undertaking to rejoin me in Paris as promptly as possible, whence we will go to Biarritz for a stay of a week or ten days. And I shall leave it entirely to you whether you prefer to come to Paris before I leave for Biarritz, or join me there on my return, when we could have a longer stay together, and possibly make a short trip to Switzerland to meet the officers of the National Bank.

Concerning all of this, please telegraph me fully, if desirable, care of the National Bank of Belgium, Brussels, as I shall be there until Tuesday evening.

Sincerely yours,

Dr. Walter W. Stewart,
care Bank of England,
London, E. C. 2, England.

Encs.

CONFIDENTIAL:Brussels, Belgium
July 29, 1925.

Dear Dr. Stewart:

This will serve to acknowledge the receipt of your message in code, received yesterday morning together with one from Mr. Jay on the same subject, reading as follows:

- "ONE Your letter indicates belief that present exchange position could be maintained with narrower differential between bank rates.
- TWO I agree, but believe that London rate, because of gold receipts, is at the moment unnecessarily high, rather than New York rate too low.
- THREE Early crop movements and seasonal requirements for currency will make money firmer in New York without rate action.
- FOUR Also prospective growth of commercial demands, if realized, will absorb some funds now in call market and have more effect than increase in discount rate.
- FIVE Believe rate advance aimed at stock market would chiefly influence bond market and further foreign flotations.
- SIX Believe rate increase in New York should await clearer indications of advance in commercial paper rate.
- SEVEN Desirable that increased use of reserve banks this autumn should largely take form of discounts rather than acceptances.
- EIGHT Suggest if action is required an advance in bill rates to level of discount rate.
- NINE Will join you in Paris after your return from Biarritz."

and to confirm my telegram in reply, reading:

"New York prefers to defer action, to which I agree. Particulars by mail."

In order to give you a complete picture, I am enclosing a copy of Mr. Jay's cable, together with a copy of my reply.

The suggestion contained in the earlier cable, originating with Mr. Young, reporting the very sudden increase in the loan account, and the possibility of a reduction to $4\frac{1}{2}$ in London, suggested at once to my mind that we might be adding fuel to the speculative situation in New York, which might later cause us serious trouble.

The coal strike in England, and the reports contained in the enclosed cable from Mr. Jay, however, make it advisable to wait, and do not indicate that present action is justified.

I am looking forward to seeing you in Paris on my return from Biarritz, and will keep you advised of the date.

With best regards, I am,

Sincerely yours,

Dr. Walter W. Stewart,
c/o Bank of England,
London, England.

P. S. As Governor Norman decided to return to London last night, you may already have gotten this picture, but you will wish to see the actual text of the messages. I am expecting the Governor to rejoin us in Paris as promptly as may be possible.

CONFIDENTIAL:

Brussels, Belgium,
July 29, 1925.

Dear Mr. Jay:

This will serve to acknowledge the receipt of your cable, received yesterday morning, reading as follows:

- *Private and Confidential. No. 4 (test) Your cable No. 3
- ONE Officers see no immediate likelihood of serious disturbance through stock exchange account. Speculation is widely difused, margins large, many large operators out of market, and most houses conservative. Volume of loans decreased slightly in last week. You have now probably received memorandum presented to Board of Directors July 16th.
- TWO Agricultural prospects excellent and general expectation throughout the entire country of substantially better business volume but no boom.
- THREE Offerings of commercial paper light but practically none being purchased under 4. Three months time money 4-1/4%. Yield on Governments working slightly higher. Borrowings here and in system practically unchanged.
- FOUR General anticipation of somewhat higher rate in early autumn. Some think commercial paper may reach 4-1/2.
- FIVE Officers think money conditions not ripe for rate increase at present and are satisfied that it would not be understood.
- SIX Therefore we recommend no action at present nor until it is clearly indicated by situation, but cannot now predict whether or when that time will arrive.
- SEVEN Have discussed business and speculative situation fully with Alexander and foregoing includes his views which coincide with ours although anything he said regarding rates was volunteered by him.
- EIGHT Alexander says present differential between London and New York private rate is not now sufficient to induce bankers here to retain money in London in view of prospect for firmer money here this autumn. He is withdrawing his funds as they mature and today declined London bid for three to six months deposit at 4-5/8% yielding 4-1/4.
- NINE If we take no action in the near future and London should now reduce, and if we should then later increase would it not seem appropriate for London if it so desired to increase again on the strength of our action at that time. This seems to us more logical and less disturbing here than for us to increase now

Brussels, Belgium
7.29.25.

Mr. Jay

(2)

- TEN Case returns August 3. Saunders and Runkle only directors available till about the middle of August.
- ELEVEN Referring to your paragraph 7 should appreciate your communicating with McGarrah and cabling his views."

and to confirm the reply which I dispatched last evening, as follows:

- "No. 4 (test) Your telegram to me No. 4
Strictly confidential for Jay
- ONE My telegram to you No. 3 reflected belief that
(a) you feared danger in stock exchange loan account as suggested your telegram to me 'bacaz' and
(b) London would reduce if we did not advance, whereas
- TWO Your telegram to me No. 4 indicates (a) is unfounded and coal strike for present defers
(b)
- THREE Suggest that you keep me advised by cable, always giving position earning assets.
- FOUR Leave for Paris tomorrow Hotel Majestic. Shall see McGarrah and cable results.
- FIVE Sending important letter to Case reporting result our talks here, copy for Winston.
- SIX All well. Regards."

It was only after my cable had gone forward that I received, via London, the batch of mail which contained the memorandum submitted to the Directors on July 16th. Concerning all of this I will write further just as soon as possible. We are leaving for Paris today, and it is not possible to do so before then.

For your information I am enclosing a copy of the message I received yesterday from Dr. Stewart in London, who has been keep in close touch with all of this information.

Sincerely yours,

Pierre Jay, Esq.,
Chairman, Federal Reserve Bank of New York,
33 Liberty Street, New York.

Enc.

8/17/25
by cable
ack
8/13/25 by letter

FEDERAL RESERVE BANK
OF NEW YORK

Paris, France,
July 30, 1925.

↓
Extra Copy of this
letter enclosed
marked -
"Copy for Mr. Winstan"
Sent W-
8/17/25
JW

Dear Mr. Case:

On reading over my separate letter to you about the Belgian situation, I notice that I have overlooked mentioning the name of Baron Terlinden as a member of the commission. He is a bank official in Brussels, and was formerly chief secretary to Prime Minister Theunis.

I do not understand that the Belgian Ambassador, Chevalier de Cartier, is a member of the commission. But the three gentlemen who are, have considerable experience in financial matters.

And, further, I find I have not given any indication of what I said to Monsieur Hautain on this subject of debt negotiations.

All that I said, in fact, was that Mr. Mellon was a man of broad experience and great skill in financial matters, and I felt sure he was sympathetic to the difficulties which Belgium had encountered and that they would find him an eminently satisfactory gentleman to deal with.

Baron Terlinden called just as I was leaving the Bank yesterday, and in the course of conversation I was casually asked what I thought would be the general line of procedure in regard to these negotiations. I told him that I had no knowledge whatever as the matter had all arisen since I left home and as it was outside of my own duties anyway, and that I could not give them any suggestions.

Sincerely yours,

Rs.

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank,
33 Liberty Street, New York.

ANSWERED
ack
AUG 13 1925
J. H. C.

C O P Y

Paris, France,
July 30, 1925.

Dear Stewart: X

I have yours of the 27th, which reached me just before I left Brussels yesterday afternoon. And I also received your telegram sent in code.

Of course, in principle, I agree with what you say about our stock exchange loan account. If fools will speculate it is just as well that they should prepare their own medicine and take it when the brew is ready. On the other hand, anything in the nature of a stock market collapse always has an adverse effect on business.

The combination of Mr. Young's suggestion, the figures of the stock exchange loan increase, the possibility of a rate reduction in London if we did not advance, the reports of our own crop outlook accompanied by easy money, and the indication that there was some optimism developing in the business outlook, led me to believe that it would be wiser for us to advance than for London to reduce; always assuming that our associates in New York were convinced that the stock exchange situation was becoming a menace.

On the other hand, the subsequent development of the British coal strike and the more reassuring report from New York regarding the exchange situation, made me feel quite content to send the cable of which I sent you a copy.

I agree with you that there is something more fundamental just now than the relation between the two bank rates, and that this movement of gold does present a difficulty. Naturally we do not want it to turn in our direction if we can avoid that. An advance in our rate, or a reduction in London, might have that effect to some extent. But I think all of us, in London, in Berlin, and in New York, must look with complacency upon a further reduction of portfolio to meet such a development if it arises. And I would not hesitate, as matters now are and with opportunity for further conversation with some of our friends abroad, to indicate to them the need of withdrawing funds from our market and earmarking gold in our vaults if they wish to save themselves the consequences of a policy which we must ourselves adopt in order to protect ourselves from too great an accumulation of gold.

All of this we can deal with much better by discussion than by correspondence or telegrams, and I am most anxious indeed to have a good visit with you on returning from Biarritz.

In view of what you say about preferring to stay in Paris until sailing time, August 25, I wonder how it would suit you to join me some time around the 10th, 12th or 13th. I am not particular as to the exact date. We could then take the three days necessary for a trip to Berne, and I would not return to London until after you had sailed. I find, as you do, that these gallops around Europe are pretty tiring, especially when we put in as long days as we did in Berlin and Brussels. And I am ready for a loaf myself.

Please drop me a line at the Hotel Palais, Biarritz. I hope you keep well and are not too tired. And with best regards, I am,

Sincerely yours,

Dr. Walter W. Stewart,
c/o Bank of England, London E. C.

*Read
with*

FEDERAL RESERVE BANK
OF NEW YORK

Rates

RECEIVED

AUG 18 1925

J. H. C.

Biarritz, France,
August 1, 1925.

ANSWERED

ack
AUG 13 1925

J. H. C.

CONFIDENTIAL:

Dear Mr. Case:

There is little to add to what appears in the letter I wrote Dr. Stewart about rate changes (copy of which went to Mr. Jay) except the cable I am sending today, of which a copy is attached.

The situation roughly appears to me as follows:

Any advance in our rate would be justified, as I understand conditions, only by our fear of a dangerous stock speculation. The report to the directors of July 16 seems to make clear that uneasiness on that score is not now justified, to a point where we should advance our rate, and that we can afford to await further developments. On the other hand, the situation in London became complicated because of their very large receipts of gold, which exceed, as I recall, 8,000,000 sterling. Their money market was easing and complaint about the high rate and its adverse effect upon trade was becoming widespread. And at the moment they were considering a reduction, the situation in the coal trade became acute and it looked as though a strike were unescapable. This led them to abandon the thought of reducing pending the outcome of negotiations.

Governor Norman returned to London from Brussels in response to a telegram stating that charges were being made that the difficulties in the coal trade were due to the resumption of specie payment, and the Chancellor wished to discuss that with him. When he returned to Paris, I found that an adjustment of the coal strike had been about agreed upon, and, in conformity with Mr. Jay's cable No. 4, paragraph 9, the Bank had tentatively agreed to a reduction to 4-1/2% next Thursday, assuming that the coal strike situation would be patched up in the meantime.

If they reduce, as I believe they will, it still leaves a differential of 1%, but probably not so great a differential as will lead to further accumulation but some reduction of American balances in London. I think they would like to have them reduced anyway, even if it becomes necessary in the fall that we should both advance our rates one-half of one per cent.

I think in the meantime it may be well to consider whether our bill rate should not be somewhat advanced; also possibly a portion of our system holdings of securities sold. This would only be for the period prior to the usual Fall demand, which may increase discounts anyway.

I am quite clear that we should not take measure to enable the banks to escape borrowing from us when the fall demand arises. It is one of the things which will keep the stock market in order to have the banks owe us pretty heavily.

Please be sure hereafter in cabling me on this or kindred subjects always to send me information of the amount that the New York City banks are borrowing from us, and of the position of earning assets in the System and in New York. This is the one item which gives a little inkling of what is going on better than any other, and, of course, an average figure is better than an actual figure as of any one date.

I am enclosing a letter addressed to Mr. Jay for you to read, also Dr. Burgess, and you can pass it on to him if you think it worth while.

Our stay in Berlin seemed to have used Dr. Stewart up. It was pretty strenuous. Governor Norman is better, but he is yet rather tired. I seem to stand the racket better than either of them.

We shall be here at Biarritz for about ten days, and then Stewart who is now in London will join me and we will try to gather something of what is going on in France. I am hoping to see the Suisse people at that time, and, on returning to London from Paris, we will arrange for a visit with both Dr. Vissering and Moll. This will cover about all the ground that it is possible for me to do without too much delaying my return.

With best regards to you and all at the bank, I am

Sincerely yours,

Reu. Strong

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank,
33 Liberty Street, New York.

Enc.

*Strong's
Trip*

CONFIRMATION OF CABLEGRAM

Biarritz, August 1, 1925.

Federal Reserve Bank,
New York.

No. 6 (test) STRICTLY CONFIDENTIAL FOR JAY

Your telegram to me No. 4 paragraph 9

ONE Norman here after trip to London. He wishes you to
know that he believes that

TWO Bank of England will reduce to 4-1/2% next Thursday
which I understand indicates

THREE Belief that coal strike will be adjusted before then
and

FOUR That this concession to trade is justified by money
market conditions

FIVE Consider this conforms to your views

SIX Send cables direct Hotel Palais Biarritz until
further notice

SEVEN All well Regards

STRONG

FEDERAL RESERVE BANK
OF NEW YORK

*Act
JHC
8/16/25*

Belgium

MADE IN U.S.A.

Hotel du Palais,
Biarritz, France,
August 4, 1925.

Dear Mr. Case:

Enclosed are some more rather hastily dictated notes; these covering the main points of our conversations with Monsieur Hautain. Please treat them as confidential. Of course they are hurriedly prepared, and I have not made any effort to get atmosphere into the notes, which would be quite impossible.

[See earlier file]

This is a delightful place, and we have had some enjoyable visits, for the Leffingwells were here on a motor trip for a few days, and the Morrors have a beautiful house about four miles from here overlooking the Bay of Biscay. Dean Jay and his wife also have arrived; they have a house in the town. And we are expecting the Gilberts tomorrow. I have telegraphed to Dr. Stewart suggesting that he come down for a few days and then we will all return to Paris next week.

Please tell Mr. Harrison I have his letters of the 21st and 24th of July and will write separately after I have had a chance to study them.

My best to all at the office.

Sincerely yours,

Ray Strong

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank of New York,
33 Liberty Street, New York City.

(Enc.)

*Copy sent to
Mr Jay 8/15/25
Copy handed to Mr Harrison
who is on his way to Wash
for Must in
Sailer
Two other copies
attached
L*

FEDERAL RESERVE BANK
OF NEW YORK

*Received
no ack necessary
H.A.B.
C. [unclear]
[unclear]*

CONFIDENTIAL:

Hotel du Palais,
Biarritz, France,
August 5, 1925.

Dear Mr. Case:

This will confirm my receipt today of your cable reading:

"No. 5 (test same as that used for No. 4)
Referring to your No. 6 to Jay:

- ONE Appreciate reason for action suggested in your paragraph 2.
- TWO Believe that principal results here of this action if taken will be further withdrawals of American deposits from London and much greater possibility of use of British credit.
- THREE We should like your estimate whenever you can make it as to whether use of British credit is likely this autumn and if so when. }
- FOUR Money now firm over first of month; discounts New York City banks \$94,000,000 and their actual reserves \$25,000,000 under requirements.
- FIVE Money rates continuing to show gradually firmer tendency.
- SIX Business and agriculture increasingly optimistic concerning autumn.
- SEVEN Present prospect is that autumn trade will draw out of town funds invested from stock market and since all the increase in street loans since January is in out of town money, this should result in stiffer rate and possible liquidation.
- EIGHT Our view now is that if there is some liquidation in stock market we can influence rate by buying securities, but this would not appear to be wise unless liquidation takes place.
- NINE Other important unknown factors are use of British credit and gold movements.
- TEN In any event it may be necessary for us to raise our rate in autumn as indicated our cable No. 4 paragraph 9.
- ELEVEN Statement from Schacht in yesterday's Times declares his intention of converting into gold the legal reserve of foreign exchange bills held by Reichsbank.
- TWELVE Is this report accurate and if so can any definite estimate be made of amount of gold to be earmarked here or exported."

and the acknowledgement which I have just dispatched, reading as follows:

"No. 7 (test)

Strictly Confidential for Case:

Your telegram to me No. 5 most illuminating. Many thanks.

- ONE Paragraph 3 - Doubt if used this year
- TWO Paragraph 9 - Likely receive some gold from London
- THREE Paragraph 10 - Judge this is not likely before my return next month.
- FOUR Paragraphs 11 and 12 - Foreign bills held by Reichsbank not over \$75,000,000, and in New York probably not over \$50,000,000. Shall ask Schacht about report, but earmarking entire amount would be negligible and possibly desirable.
- FIVE Harrison's letter of July 21 - After consulting Norman believe within legal limitations proposed form is best available."

It was a great satisfaction to have so prompt and complete a cable from you, and I hope you will continue to keep me advised.

I hope that you have returned after a good holiday, and that Jay got off as he had planned.

This is a delightful place, and as the weather keeps fine, we are enjoying it immensely. Dr. Stewart will join us on Saturday, and then the middle of the week we will leave, Norman returning to London, and we going on to Paris, where I hope to have some good visits with Governor Robineau.

My best to all at the office.

Sincerely,

Reis: Aronq

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank of New York,
33 Liberty Street, New York.

Stewart's
Trip

Hotel du Palais,
Biarritz, France,
August 7, 1925.

Dear Mr. Harrison:

Thank you for your fine letter of July 21.

After discussing it with Governor Norman, I cabled (paragraph 5 of my cable No. 7, separately confirmed)

"After consulting Norman believe within legal limitations proposed form is best available."

He feels, as I do, that the limitations of the statute are such that we can do no better than is proposed in the memorandum you sent. And I feel myself that the inference to be drawn from our published figures will not only do no harm, but will probably not be available to most readers because it requires a comparison of two separate statements, published at two different times; that is, the weekly statement of condition, and the maturity statement of bills published in the Bulletin; and that little danger is to be apprehended. Besides that, we may be buying other foreign bills long before the British credit is used.

The situation seems to be that gold is piling up in the Bank of England, so that they are about to 168,000,000 sterling, while the Cunliffe report only suggested a minimum of 150,000,000 sterling.

Governor Norman feels that he cannot well advance his rate until after he has shipped some gold. I disagree with him as to this, because I feel that the present time is the opportunity which the Chancellor should avail of to increase the gold behind the currency notes, which has something the same effect as a gold shipment, and which will strengthen the Bank against the time, say two years or more hence, when it will assume the currency note issue in toto.

They probably reduced their discount rate yesterday, although we have no advice as yet. And Governor Norman anticipates, as I do, that if an increase on the part of either is found necessary in the fall, it will mean that he must advance to 5-1/2% if we advance at all; but that if he advances it may not be necessary for us to do so, even though the differential between London and New York is thereby increased.

We are reserving final discussion of these matters until Dr. Stewart gets here tomorrow.

We are having a good vacation now, although the stay at Spa was

Biarritz, France
8.7.25

Mr. Harrison

(2)

a distinct failure. The weather was bad and the place dull. Here it is quite the reverse, and the climate is splendid.

I will write you separately about the inquiry data, which I have not yet studied.

Sincerely yours,

George L. Harrison, Esq.,
Deputy Governor, Federal Reserve Bank of New York,
33 Liberty Street, New York.

*ack
JMC
8/11/25*

FEDERAL RESERVE BANK
OF NEW YORK

RECEIVED

AUG 28 1925

J. H. C.

CONFIDENTIAL:

Hotel du Palais,
Biarritz, France,
August 11, 1925.

Dear Mr. Case:

I have your cables numbers 7 and 8, as follows:

"No. 7 (test o.k.)

- ONE Your telegram to me No. 7
If Reichsbank expects export gold from New York and London may ship us, perhaps you, Norman and Schacht could arrange for direct shipment London to Berlin, or earmarking in London, with settlement here in either case, which will help them and have same result here.
- TWO Your letters July 15, July 19, two July 20, two July 21, and July 23 to Jay and Case received and read with much interest.
- THREE Referring to your letter of July 20 to Jay concerning Rentenbank and Mitchell, Jay left August 1 for vacation in Canada and had no opportunity to see Mitchell. We understand Mitchell sailing for Europe and therefore consider it unnecessary to discuss this matter with him since he will undoubtedly obtain information himself first hand.
- FOUR Referring to your second letter of July 20 to Jay concerning possibility of our buying mark bills from Reichsbank, most of our directors out of town until after middle of August when I will discuss situation with Young, Woolley and others interested."

"No. 8 (test o.k.)

Your letters July 28 and July 30 about Belgian situation received Friday, August 7, and copies sent immediately to Winston who was pleased to receive them as first meeting with Belgian Commission took place today."

to which I am replying:

"No. 9 (test) Strictly Confidential for Case:
Replying to your telegram No. 7 by mail.
Thanks your telegram to me numbered 8."

As to No. 7, I think the announcement of Dr. Schacht's policy will not likely result in any exports from New York. His announcement was,

in fact, somewhat inspired by his talk with Governor Norman and me, wherein it was pointed out to him that if his reserve continued to remain inflexible and was constantly maintained three-quarters in gold and one-quarter in foreign bills, he would be educating the public to a state of mind in regard to his reserve which might cause trouble whenever the need for a reduction occurred; that is to say, either a reduction in the total, or in either one of the respective items.

In order to meet this criticism, he is proposing to give it a fluctuating quality right away, by arbitrarily increasing and decreasing the gold proportion. This means that there may be times when he will earmark some gold with us, and later will invest it through us.

As to short-routing gold from London to Berlin, Governor Norman and I feel that it is unlikely that this can be done. The Bank of England does not propose itself to ship any gold. Such gold as might be shipped would be taken from the Bank by the market and shipped purely as an exchange operation.

It is possible that I shall see Dr. Schacht later, before returning home, when I can suggest that he have it in mind that something of this sort might be worked out between himself and Governor Norman to save some uneconomical double shipments of gold. And if I find that I am not going to see him, I will write him about it.

Dr. Schacht is likely to go to New York in October or November, and we can talk this over then.

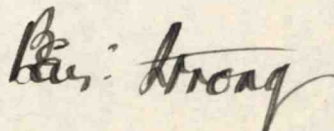
Colonel Logan joined us here yesterday, and from him I learn that Mr. and Mrs. Charley Mitchell are now in Paris; and I am expecting to meet them at dinner on Friday of this week. This may afford the opportunity to discuss the Rentenbank matter with him.

The possibility of buying mark bills is, of course, pretty remote. My letter was simply intended to get thought started on the subject.

We all keep well and are enjoying our visit here at Biarritz.

Best regards to you all.

Sincerely yours,



J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank of New York,
33 Liberty Street, New York.

FEDERAL RESERVE BANK
OF NEW YORK

RECEIVED

AUG 22 1925

J. H. C.

Hotel du Palais,
Biarritz, France,
August 12, 1925.

Dear Mr. Case:

This is to acknowledge the receipt of your cable,
as follows:

"No. 9 (test o. k.) Confidential:
A. C. Miller telephones New York Counsellor of
Italian Embassy is making inquiry of him as to
your whereabouts and whether you plan visit to
Italy. Miller thinks inquiry from Mussolini
and, at my suggestion, is replying you are now
vacationing and not planning such visit.
Italian Embassy wants your address. Please
cable whether we should encourage or discourage
them."

and to confirm the reply which I have just dispatched, as fol-
lows:

"No. 10 (test) Your telegram to me numbered 9:
Say I am not planning visit to Italy and return
home after short stay at Paris and London."

We have had an enjoyable stay here, and leave in the morning
for Paris, where I shall be at the Hotel Majestic for ten days or two
weeks prior to returning to London. Governor Norman, however, returns
home tonight.

My best to all at the office.

Sincerely yours,

Beng Stoung
—M.S.B.

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank of New York,
33 Liberty Street, New York City.

FEDERAL RESERVE BANK
OF NEW YORK

W. H. C.

CONFIDENTIAL:

Hotel Majestic,
Paris, France,
August 15, 1925.

7/30/25

Dear Mr. Case:

Referring to your cable in regard to the Reichsbank's possibly taking more gold, I am sending you with this a letter which I have just received, after much delay, from Mr. Gilbert, together with a copy of the statement, a portion of which appearing in the press doubtless suggested your cable to me.

I am told very confidentially indeed that the occasion for this statement was a request by the Chancellor that the Reichsbank reduce its rate to 7%. This Dr. Schacht explained could not be done, and he immediately called a meeting of the Central Committee of the Reichsbank and submitted the statement of July 29, which was unanimously approved and then went to the press.

This does not necessarily indicate any lack of harmony between Dr. Luther and Dr. Schacht, but it does afford evidence of the vigor with which Dr. Schacht is endeavoring to maintain the independence of the Reichsbank, which in fact was one of the essential principles set out in the Dawes Plan.

I am sure that Mr. Young will be interested in reading this, and you may, therefore, show it to him in confidence.

Sincerely yours,

W. H. C.

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank,
33 Liberty Street, New York.

Enc.

RECEIVED

AUG 29

J. H. C.

WATERMILL
BOND

MADE IN U.S.A.

2/20/25
X Mitchell

FEDERAL RESERVE BANK
OF NEW YORK

Hotel Majestic,
Paris, France,
August 18, 1925.

Dear Mr. Case:

Many thanks for yours of the seventh, received yesterday.

There is still a chance that I shall see Mr. Mitchell when I am in London, and I am sorry that there was a misunderstanding about his arrival here. The fact is I was invited to dinner to meet him last Friday night, it having been understood that he would arrive here Thursday of last week, instead of which he is in London this week.

Of course I shall await with interest whatever you learn about his statement to the Department of State in regard to our business in Prague. If he has gratuitously, or in any other way, undertaken to make any trouble through the Department of State, I will be inclined to take it up, on my return, with the bank officially. For that sort of thing we certainly cannot tolerate. I hope that his explanation was sufficiently convincing to make this unnecessary. Of course if I see him I shall ask him to tell me what it was all about.

This, of course, leaves the matter of the directorship up in the air, but I shall await something further from you before doing anything.

About a possible purchase of mark bills: I regard the transaction as extremely unlikely, partly because there has recently been a considerable improvement in Schacht's devisen position, and partly because of his obvious reluctance to obtain credit by that method. My letter, as stated, was just a preliminary warning, so that you could be thinking it over.

The criticisms at home could be ignored were we to limit our transactions to purchases of bills, without any agreement for renewals.

I shall write nothing in general about conditions until I reach London, which will be about the 28th of this month. My present plan is to sail on the Olympic on the ninth. That's about the best that can be done without pushing too hard and fast and coming home tired out.

Thursday night Dr. Stewart and I are going up to Switzerland to spend one day and one evening. We will be back here on Saturday evening.

I had a most interesting lunch at the Bank of France yesterday, with endless courses. But nothing of special interest developed, except that the members of the Council were all most interested to learn whatever I was willing to tell them about affairs in Germany, - which was not much - and they were especially keen to impress upon me the desirability for lenient treatment in the debt negotiations. Concerning this I said that I had no official responsibility and felt that the best thing to do with that question was to settle it, and not to let it remain a bone of contention.

Paris, France

FEDERAL RESERVE BANK OF NEW YORK.....8.18.25..

Mr. Case

(2)

I had another meeting at the Bank this morning, and one for Thursday afternoon, when Robineau and I will have a chance for a private talk. I will write you anything that develops.

Best regards to you all at the bank.

Sincerely yours,

Benj. Strong

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank of New York,
33 Liberty Street, New York City.

FEDERAL RESERVE BANK
OF NEW YORK

Hotel Majestic,
Paris, France,
August 20, 1925.

*see file
Norman
8/17/25*

Dear Mr. Case:

The enclosed letter, just received from Governor Norman, and the translation from the "Frankfurter Zeitung" explain themselves. I think you will find them interesting reading. Won't you pass them along to the officers, and possibly you will also ask Dr. Burgess to glean what he may from it as an aid in talking to the newspaper men. Then it can be passed back into my files.

Sincerely yours,

W. H. C.

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank of New York,
33 Liberty Street, New York.

Encs.

RECEIVED

AUG 29 1925

J. H. C.

BANKERS IN BERLIN.

"BERLIN, Friday.- Mr. Montagu Norman, the Governor of the Bank of England, and Mr. Benjamin Strong, the Governor of the Federal Reserve Bank of New York, arrived here this morning to negotiate with Dr. Schacht, the President of the Reichsbank.

"Dr. Schacht stated, in an interview, that the conversations were not to be about a loan, but it is believed in financial circles that they will concern the possibility of further German private loans, from abroad.- British United Press."

DAILY MAIL

July 11, 1925.

MR. MONTAGU NORMAN,
GOVERNOR OF THE BANK AT BERLIN CONFERENCE.
FROM OUR OWN CORRESPONDENT.

Berlin, Friday.

"The Governor of the Bank of England, Mr. Montagu Norman, and the Governor of the Federal Reserve Bank of New York, Mr. Benjamin Strong, have arrived at the Hotel Adlon here.

"It is announced that they are having conversations with the President of the Reichsbank, Dr. Schacht, regarding business relations between the three banks."

WESTMINSTER GAZETTE

July 11, 1925.

CENTRAL BANK GOVERNORS MEET.

"The joint visit to Germany of Mr. M. C. Norman, the Governor of the Bank of England, and Mr. Strong, the Governor of the Federal Reserve Bank of New York, as cabled from Berlin, will probably not come as a surprise even to those who were unaware that such a visit was under contemplation. Dr. Schacht, the President of the Reichsbank, has lately been faced with a complex financial situation in Germany, which has been aggravated by the crisis in the Stinnes Trust. It will be recalled, moreover, that the immense importance of German foreign trade for the purpose of carrying out the Dawes Plan was particularly emphasised at the recent session of the International Chambers of Commerce in Brussels. The figures of the trade balance to date have been far from satisfactory, and Dr. Schacht, in addressing the Federation of German Industries in Cologne just lately, made a similarly significant reference to the necessity for Germany to meet her obligations abroad. In regard to the demand for credit, which has been greatly restricted, Dr. Schacht has declared that, whilst recognising the great need there is for credit the economic situation does not permit of its being provided. In view of the growing uneasiness in the industrial and business communities in Germany and other indications, the conference of Central Bank representatives may prove a timely aid."

ENGLISH AMERICAN VISIT AT THE REICHSBANK

Our Berlin office writes to us; the Governor of the Bank of England, M. Norman, and the Governor of the American Federal Reserve Bank, B. Strong, are visiting the Reichsbank President, Dr. Schacht, in Berlin. They intend, as the Reichsbank direction declares, to discuss with Dr. Schacht the relations which arise from the natural intercourse of their institutions. It is natural to assume that the relations, in particular, will also be discussed which have arisen with England and America in regard to the Gold-diskont-Bank. As is known all the shares of the last mentioned, after the payment of the sums put up by the Bank of England went into the hands of the Reichsbank which also manages it. In April of this year it was decided to make the bank, which had become meaningless as a currency institution, live again as a purely credit institution. The intention was, chiefly by granting credit to the exporting industry, to help this along, the secondary intention was in this way to secure a better rate of interest for the external possessions of the Reichsbank. The old credits of the Golddiskontbank, which at the end of last year amounted to 6.7 millions pounds in drafts and checks had been reduced in April to about 3 millions and should be fully wiped away in the later intervals. On the other hand new credits to the amount of 5-6 million pounds have been given, which, for that matter Dr. Schacht, before the Kolner meeting had also mentioned. Lately, as we hear the credit amounts are again very numerous and the exchange amount is slowly rising. In connection with this they will think perhaps in the Reichsbank of regarding more the rediscount possibilities in foreign parts. We are inclined to assume that the presence of Messrs. Norman and Strong, has a certain relation to this. As we at the time stated the foreign rediscounters (in the first line also the International Acceptance Bank) had declared that they would take up again the credit relations to the Golddiskontbank after the rediscount credit of 25 million dollars that was previously certified to, and, that could hardly be taken into account, was declared off on December 15th of last year. We may therefore, assume that now relations with London and New York have been taken up again with the object of a renewal of the rediscount credit to the German Golddiskontbank.

BERLINER BÖRSEN-ZEITUNG

July 11, 1925.

THE BANK PRESIDENT'S OF NEW YORK AND LONDON IN BERLIN

Conversations with Reichsbank President Schacht.

In financial circles great importance is given to the visit of the President of the Bank of England and of the Federal Reserve Bank of New York to the Reichsbank President, Dr. Schacht, in Berlin, the more because silence is kept guarding the object of the visit. The rumor is spread however, that it is a question of negotiations for a new German loan.

The "British United Press" publishes an interview of its correspondent in Berlin with the Reichsbank President, Dr. Schacht, he is said to have declared that Montague Norman, and Benjamin Strong have come to Berlin to visit him personally and to talk about certain circumstances which have to do with the relations between the three national banks. At any rate Dr. Schacht had categorically denied that the transaction had any thing to do with a new German loan.

8 Uhr-Abendblatt

July 15, 1925.

RUSSIAN GOLD IN LONDON

Lately in London there has been a Russian sending of gold of the value of 20,000,000 marks for the payment of English machinery delivered in Russia. Our picture shows the London Custom Officials examining the gold cases.

July 15th Mr. Case.

TRANSLATIONS OF CLIPPINGS SENT BY GOVERNOR STRONG TO MR. CASE

BERLIN TAGEBLATT - Making the Dawes Plan Sure. The Berlin Consultations of the Bank Presidents. Washington, July 14. The Philadelphia Public Ledger today points out the great significance of the present Berlin consultations of Bank Governors Strong and Norman. "It is clear," writes the newspaper, that these leading financial authorities do not intend to inform each other about weather conditions or turtle eggs from Timbuctoo, but are preparing decisions of the greatest importance for the financial fate of the world." The making sure of the Dawes plan stands in the foreground of interest and the necessary preparatory measures for this must be taken at the right time. The present Berlin conferences will be followed by numerous ones of similar nature till conditions attain a common definite stabilization.

BERLIN TAGEBLATT - America and the Transfer Question. Washington, July 13. The leading New York commercial newspaper, "Journal of Commerce," speaks, under the heading "Mysterious Finance," of the Berlin journey of the Governor of the Federal Reserve Bank in New York, Strong, in company of the Governor of the Bank of England, and writes: "Since England has returned to the Gold Standard, it is no longer able to hold Germany under the arms with credits as liberally as before, and America's help is therefore necessary for the solution of all the currency problems that arise in connection with the carrying out of the Dawes plan. Difficulties of transfers could only be overcome by securing shortterm credits. In this it is a question of technical transactions, the carrying out of which would be not at all in contradiction with the American policy of keeping away from the entanglements of the Reparations question." The newspaper demands that all necessary bank operations in this connection should be carried out on a strictly legal basis, in order that there should not again be a protest of the American Congress, as there was in the case of the restoration of the English currency to the gold standard. America has every interest in Germany's returning to sound currency conditions, as England has.

VOSSISCHE ZEITUNG - America on the Visit of the Bank Presidents. New York, July 13. The visit of Norman and Strong to Schacht has interested greatly the New York banking circles. The most varying versions as to its object are in circulation. The simplest explanation is that Germany seeks an additional loan to the Dawes loan. The second explanation is England is so embarrassed by the return to the gold standard that she needs for herself the resources which she formerly placed at Germany's disposal, and on that account Strong wishes to inform himself in order to come to England's assistance. This would especially concern a German short term credit affair and the exchange discount. The third version, finally, asserts that in connection with the transfer question, the foundation of branches of the combined general reserve banks in Germany and perhaps in England also, is planned.

TRANSLATIONS OF CLIPPINGS SENT BY GOVERNOR STRONG TO MR. CASE.

FRANKFURTER ZEITUNG - Interview of the Note Banks. Our Berlin correspondent writes: It is undoubted testimony of a great moral success of the young Reichsbank, that it could receive the visit of two leading note bank heads, two persons, to wit, who are not imbued with the quality of controllers or of creditors, but are simply the representatives of the currency banks of their countries and as such wished to confer with the currency bank of another country. Mr. Strong of the Federal Reserve Bank of the State of New York came, on his European journey, to the Bank of England, and the lately reelected Governor Norman of that bank, for a long time conversant with German problems and German personalities accompanied him on a journey to Berlin; apparently the visit had no practical business or currency tactics object, but instead the purpose of drawing closer the present contact, and of talking over all subjects which today can interest the note bank heads of important countries that are related to each other in the general rearrangement of world and money economics; among these the Transfer problem and the questions for the year 1926 are said to have been discussed. The conference lasted many hours and the parting was in a very cordial tone, if a chance observer might judge. They clearly gave each other full information; especially was that done from the German side and conscientiously; they undoubtedly agreed unanimously in their views and in the currency policy; only in this way can mutual understanding be secured for the case, that some time later - not now - international financial questions of importance may be solved by mutual consent. To speak of credits and loans as a subject for the conference is naturally absurd. It is amply sufficient when the guests carry away with them a good impression of the common sense with which bank policy here is handled, and of the earnestness with which German industry is striving to bring about its reformation and its readaptation. From convictions obtained personally alone can support be found for German private credit abroad, which later, especially when lands come into contact again, are of greater use than any present agreements, which would have to count on the difficulties of foreign markets.

Translated by -
G. Bendelari
July 27, 1925.

GERMAN PRESS OF JULY 13/14, 1925.

I. DAWES PLAN AND REPARATIONS.

(a) The Vossische Zeitung and Berliner Tageblatt of July 14, 1925, publish information concerning the visit of Mr Montagu Norman and Mr Strong to Dr Schacht.

The Vossische Zeitung draws attention to the interest aroused by this visit in New York financial circles and to the different reports current as to its object. The simplest version of these is that Germany wishes to raise an additional loan to the Dawes Loan. It is also said that, owing to the return to the gold standard, England now requires in toto the funds previously placed by her at Germany's disposal and that Mr Strong desires to collect information with a view to supporting Great Britain. According to a third version, the foundation of branches of all the Federal Reserve Banks in Germany and perhaps also in Great Britain is under consideration, in connection with the Transfer problem.

The Berliner Tageblatt quotes from an article from the Journal of Commerce, dealing with Mr Strong's journey to Berlin and entitled "Mysterious Finance". The assistance of the United States has become necessary for the solution of the various currency problems connected with the application of the Dawes Plan. The transfer difficulties can, it is argued, only be overcome by the issue of short-term loans. These would consist of technical transactions, the execution of which would not be incompatible with American policy, the object of which is to hold aloof from any interference in the Reparation question. The Journal of Commerce urges that all banking operations should be carried out on a strictly legal basis.

(b) The Boersen Courier, evening edition of July 13, 1925, publishes a report stating that the Journée Industrielle has made public a statement by the Under-Secretary of State for the Liberated Regions, M. Schmidt, confirming his intention of substituting new regulations for all existing regulations regarding deliveries in kind by Germany. His object is to simplify these deliveries.

(c) The German Delegate, Herr Lehnhardt, and M. Sartini, Belgian plenipotentiary, have signed in Paris an agreement under which Germany will pay an indemnity of 24 million francs to Belgian subjects deported during the war. According to the Berliner Tageblatt this indemnity was offered spontaneously by the German Government. The indemnity will be distributed among 55 000 Belgian subjects, i.e. an average of 450 francs per person.

(d) The Deutsches Tageblatt (Fascist) of July 14, 1925, states that the economic disaster threatening Germany is "the benediction of the Dawes Plan". The Deutsche Zeitung expounds the difficulties involved in the settlement of reparation payments which were recognised at Brussels. These difficulties confirm the arguments put forward some time ago by the Deutsche Zeitung and its financial correspondent, Herr Bang. The Deutsche Zeitung displays satisfaction with the comments of the more moderate German Press upon the Brussels Conference.

II. CREDITS.

(a) The Vossische Zeitung reports that a certain portion of the City of Berlin Loan is being offered on the Amsterdam Bourse. The prospectus of the Loan contains the statement that the service of the City of Berlin's debts will not exceed in all 4 300 000 dollars per annum. It is impossible to give more exact particulars pending the final settlement of the revalorisation question. The charges resulting from the Dawes Plan for the Berlin communal undertakings are estimated not to exceed 475 000 dollars for the year beginning September 1, 1925, 590 000 dollars for the following year and 1 150 000 dollars for the succeeding years.

(b) The Muenchener Neuesten Nachrichten state that the negotiation of the Bavarian Loan is being conducted at Munich with a prominent delegate of a group of New York banks.

According to the Boersen Zeitung, the City of Bremen has not suspended negotiations with American finance. It proposes to contract a foreign loan, independent of the 11 million mark loan granted by the mortgage banks.

(c) The Deutsche Handelsdienst confirms the report regarding the forthcoming flotation of the loan contracted by the Glanzstoff Group (German) in the United States. The principal of the loan is for 3.5 million dollars.

III. COMMERCIAL POLICY.

(a) The Vorwaerts announces from Warsaw that the Polish Commercial Delegation has offered to resume negotiations with the German delegates. The German Government's proposals are to be re-examined and counter-proposals will be submitted.

A new decree published by the Polish Government lays down certain new import prohibitions. The decree is to come into force on July 17, 1925, and will apply to a large number of German products.

(b) The Commercial Committee of the Reichstag discussed yesterday, July 13, 1925, the tariff items in the Customs Bill relating to the iron producing industry. The Socialists and Democrats criticised the Government's Bill, the former pressing for the withdrawal of the duties and the latter for their reduction.

The German Civil Servants' Union has published a manifesto protesting against the Customs Bill, the application of which will, in their opinion, conduce to a general increase in the cost of living, economic confusion and social controversies. The Union, on behalf of one million Civil Servants, is opposed to the minimum duties on cereals.

IV. ECONOMIC.

(a) The last remaining obstacles to the foundation of a German Steel Trust were overcome at a plenary meeting of the members of the "A" Products Union (semi-finished products, laminated iron, railway material). (Deutsche Allgemeine Zeitung, July 12, 1925)

(b) According to the Kölnische Zeitung, the German railways will commence in November the work of completing or renewing their stock of locomotives.

(c) According to a report in the Vossische Zeitung, Mr Harriman and the General Manager of the United American Line have left for Hamburg, where, it is said, they are to negotiate as regards the possible purchase of the Stinnes fleet.

(d) The A.E.G. will be entrusted by the City of Berlin with the construction of the new electric power house at Rummelsburg. The sum involved is over 50 million marks.

V. FINANCE AND TAXATION.

(a) In its meeting on July 13, 1925, the Taxation Committee of the Reichstag continued the debate on the Finanzausgleich Law and adopted the motion submitted by the Government Parties on the increase in the Beer Tax. The amendments were all rejected. The Government representative estimated the yield of the new tax at 40 or 45 per cent more than the old tax. The debate on the Tobacco Tax has commenced. A Socialist deputy and a Democratic deputy protested against the increase in the latter tax.

(b) In the Vossische Zeitung, Dr. Flügler, Syndikus of the Cigarette Trust, protests against the proposed Tobacco Tax and states that in its present position the cigarette trade is unable to support heavier burdens. Dr. Flügler recalls the proposals made by the trade with a view to settling the question of the tax by a Steuergemeinschaft (joint committee of the trade on taxation).

The Berliner Tageblatt of July 14, 1925, publishes an article by the Syndikus, Herr Breuer, calling attention to the excessive taxation borne by the German champagne (Sekt) industry.

The Vorwaerts of July 14, 1925, protests against the proposed regulations for the tax on rents.

(c) The Reichstag concluded on July 13, 1925, the second reading of the Law on the revalorisation of mortgages. The proposed prescriptions for the revalorisation of industrial bonds were adopted.

(d) A summary return of staff in the Ministries of the Reich, in the Postal Administration, and National Printing Press, has been laid before the Reichstag. The Ministries of the Reich employed on April 1, 1925, 95 789 civil servants, 21 163 lower grade officials and 44 653 workmen. The Postal Administration and National Printing Press have in their employ 252 585 civil servants, 3 254 lower grade officials and 38 447 workmen. These figures are slightly lower than those for October 1, 1924.

VI. POLITICAL.

(a) The Cabinet will meet to-morrow to discuss the reply to M. Briand's Note.

The German Government has collected and published, ⁱⁿ a pamphlet of about 100 pages the principal documents relating to the security question.

During his visit to Dresden, the Chancellor, Dr Luther, informed the journalists that the Government had not yet taken a decision as regards the Provisional Reply to be sent to M. Briand. The German Note would, he said, refer to each of the various legal points introduced into the discussion by the French Note.

(b) The Vossische Zeitung, evening edition of July 13, 1925, expatiates on the opposition shown by the Nationalist Party to Dr Stresemann. / ~~the~~ forthcoming resignation of Dr Stresemann from the Ministry for Foreign Affairs has been current in certain circles, but is denied by the Taegliche Rundschau of July 14, 1925. The Berliner Tageblatt recognises that Dr Stresemann's position is threatened.

A report
concerning

VII. NEWS ITEMS.

The Vice-President of the United States, General Dawes, gave a banquet in Chicago on July 13, 1925, on the occasion of the visit of the German Ambassador, Herr von Maltzan. Speeches were delivered by General Dawes and the Ambassador. (Berliner Tageblatt)

The French Chamber of Deputies has passed the 1925 budget by 421 votes to 150. The Socialists voted against the Budget. The German Press regards this vote as the end of ~~the~~ "cartel des gauches".

Preparations for evacuation are being actively pursued in the Ruhr. A first zone will be evacuated this week.

The Congress of the German Chambers of Commerce and the Aircraft Manufacturers' Trust have protested against the last note from the Council of Ambassadors.

A strike has broken out in the building trade in Berlin, involving about 25 000 workers.

From the French
Translated - CP
Checked - NL

MH.

CREDIT PRESSURE ON THE AGREEMENT PROCEEDINGS?

London, July 16, 1925.
Private Report.

"Daily Herald" has it telegraphed to it that Montague Norman, the Governor of the Bank of England, who is now staying in Berlin, has promised Germany a credit of 40,000,000 pounds, if it accepts the alliance proposal of Briand, endeavors to be taken into the alliance of nations, and pledges itself to support England's policy against Russia."

That is naturally a piece of news with a purpose that can be easily seen through. A notice in the "Times" is probably to be taken seriously, on the other hand, which repeats a large number of the excuses brought out in Germany against the security agreement and finally ends with the opinion that the care for foreign credits outweighs everything, but that these foreign credits cannot advance without a solution of the security question. Further a notice of the diplomatic correspondent of the "Daily Telegraph" must be mentioned, who writes: "After the English-German commercial treaty has been held up the opinion will rule strongly in London that Germany should be refused credits as long as the wishes of England are not complied with."

We do not believe, indeed, that this wish, in fact, is held in earnest in London. From the preceding news items, however, it is clear to be seen how sure people in London are that they can obtain everything from Germany if only they offer credit to it. This idea is naturally helped by Germany herself. It is not devoid of danger for Germany because in it the position of Germany seem much weaker than it really is. As a matter of fact, in Germany, from the beginning, the possibility of building up again its own economic conditions with foreign credits has been exaggerated in an extraordinary manner. In the second place England's economic position is such that a dropping out of the German consumer, through a cutting off of credit, would injure English business for natural reasons to a degree that England could not support in her present condition; and finally it seems that people do not clearly see whether a credit boycott organized by England must of necessity lead to an organized ware boycott on the part of Germany which would deal many wounds to English commerce.

THE VISIT OF THE BANK GOVERNORS

Montague Norman's and Benjamin Strong's Berlin Transactions.

On the 10th of July, ~~has~~ has been stated the Governor of the Bank of England, Mr. Montague Norman, and the Governor of the Federal Reserve Bank of New York, Mr. Benjamin Strong, arrived in Berlin. Both gentlemen, who are at the head of the English and the most important American banks of issue, have made a visit of several days on the Reichsbank president, Dr. Schacht, here, which at present is still continued; have had several conferences with him and other important persons and have partaken of several common meals. This visit has given rise to a number of comments and suppositions in this country and in foreign parts which are partly erroneous. Among other things a connection with

The Termination of the First Dawes Year

in August, with questions of transfers, and with the use of the fund created by the reparations loan, has been imagined, and further and more extensive suppositions have been attached to this apparently accidental visit. On the other hand it must be established that the personal visit of the two Governors of banks of issue has no especial or peculiar cause, and that people have little cause for astonishment in it because in future more of such conferences will take place. The solution of the reparations question, and the stabilizing of German currency is built out of the London agreement, this again out of the contents of the Dawes Plan; the Dawes plan on its part assumes the creation and the keeping up of a stable German currency, if it is to be carried out, and intends in this connection to have a strengthening of the Reichsbank.

In the plan itself and in the Reichsbank law, it is expressly stated that a friendly cooperation of the various foreign banks of issue, which are represented in the general council of the Reichsbank, and took part in leading to the emission of the reparations loan, should be assured. That compels the settlement of a whole series of mostly technically executive or banking questions; among other things they are to be consulted in the case of replacing a departing member of the general council. Moreover it must be established that the Genoa Conference had already given the banks of issue and their working together a certain part.

The Reichsbank president, Dr. Schacht

who, has come into touch with the two gentlemen that are dealt with here about the proceedings of last year, has consequently kept their visit in agreement with the problems that existed before hand, which the Reichsbank has inherited on the one hand through the agreements built upon the London agreement, and on the other hand through the relations of the German bank of issue to international finance and to the foreign banks of issue. Dr. Schacht, as is well known, made a visit to Brussels some time ago, and it is to be assumed that the Governor of the Belgian bank of issue, Mr. Hautain, will also at the proper time speak in Berlin in return for this visit. From all such conferences the conclusion is perhaps to be drawn that there will be a more intelligent and active cooperation of the bank of issue institutions which deal with the currencies of the individual countries, but not that there will be special consultations in every single instance which could have a definite object or perhaps a political meaning for the country that is visited at the time.

THE VISIT OF THE BANK GOVERNORS

On the 10th of July the Governor of the Bank of England, Mr. Montague Norman, and the Governor of the Federal Reserve Bank of New York, Mr. Benjamin Strong, arrived in Berlin. The two gentlemen, who are at the head of the English and of the most important American banks of issue, have arranged here a visit of several days, which is still continuing, with the Reichsbank president, Dr. Schacht, have had various conferences with him and other important persons, and have taken part in some common meals.

This visit has given occasion to a number of commentaries and combinations in this country and foreign parts, which are partly erroneous. For example, a connection with the ending of the first "Dawes Year" in August, with questions of transfers, and with the use of the fund created by the reparations loan, have been made out, and still further suppositions have been connected with this probably accidental visit. In opposition to this it may be assured that the personal visit of the two bank of issue Governors had no special or extraordinary cause, and that people have even so little cause to be astonished at it in that, in the future, more such conferences will take place. The solution of the reparations question and of the German currency stabilizing is grounded on the London agreement, and this again on the contents of the Dawes plan; the Dawes plan on its part assumes the creation and the maintenance of a stable German currency in order to be carried on, and aims in this connection at a strengthening of the Reichsbank.

In the plan itself and in the Reichsbank law it is expressed, that a friendly working together of the various foreign banks of issue, which are represented in the general council of the Reichsbank and which were already leading in the giving out of the reparations loan, shall be assured. That is surely necessary for a whole series of questions of technically executive or banking character; among other things they are to be consulted in the choice of a successor to a departing member of the general council. Moreover it must be established that the Genoa conference gave to the banks of issue and the common work a certain part to play.

Reichsbank president, Dr. Schacht, who has come into closer connection with both the gentlemen in question here in relation to last year's dealings, has therefore kept their visit in consonance with the standing obligations, which the Reichsbank, on the one hand through the agreements built upon the London agreement, and on the other hand through the relations of the German banks of issue to international finance and to the foreign banks of issue, has assumed. Dr. Schacht has, as is known, some time ago made a visit also to Brussels and it is to be assumed that the Governor of the Belgian bank of issue also, Mr. Hautzin, will make an address in Berlin, as a return for this visit. From all these conferences the conclusion to be drawn is perhaps of the development of the more intelligent and active cooperation of the bank of issue institutions, responsible for the currencies of the individual countries, but not of special deliberations in each individual case which would have a definite object or political significance for the country that was visited.

BERLINER TAGEBLATT

July 16, 1925.

FALSE NEWS OF A NEW 400 MILLION LOAN FOR GERMANY

Foreign newspapers state that the President of the Federal Reserve Bank, Strong and the President of the Bank of England, Norman, who are at present in Berlin are dealing with the Reichsbank president, Dr. Schacht, concerning the assurance of an English American loan of 20 million pounds sterling, which apparently are to be given to Germany as soon as the security agreement is signed. This news, which sounds very improbable event to a particularly informed reader, is declared from a reliable German source to be false.

FEDERAL RESERVE BANK
OF NEW YORK

Hotel Majestic,
Paris, France,
August 24, 1925.

Dear Mr. Case:

Governor Strong asks me to hand you this copy of his letter to Mr. Winston, the original of which Dr. Stewart is carrying to him by hand, as, indeed, he will carry this to you. It gives about everything in the way of impressions, etc., that Governor Strong can send at the moment, and he is sure you will be interested in it. It is, of course, confidential.

We leave Paris on Friday morning, August 28, for London, and thereafter cables may be addressed to the Bank of England in the usual course.

Very truly yours,

W. S. Bleecker

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank,
33 Liberty Street, New York.

Enc.

CONFIDENTIAL:

Hotel Majestic,
Paris, France,
August 19, 1925.

My dear Winston:

So far, I have not had opportunity to gather impressions in France as fully as I would like, partly because so many people are away on vacations, and partly because of language and other difficulties which have to be overcome here to a greater degree than almost anywhere else in Europe.

Undoubtedly they have had a good crop this year, and it is now pretty well gathered. I refer especially to cereals. The tourist crop has been about the best on record, and, from personal experience, I can testify that it has brought a good price. In Paris, even on a gold basis, prices are pretty high, and yet Americans have been here in droves, spending money right and left.

Of course there has been a good deal of uneasiness about the situation in Morocco, but the evidence of cooperation between the Spanish, British and French, and the recent military success which the French enjoyed against the riffis has largely relieved that feeling of uneasiness, which was undoubtedly growing and having a rather widespread effect.

There is unfortunately some feeling that when Parliament reassembles the present government will be facing difficulties which they may not be able to survive. Two or three people have mentioned to me the possibility of their not lasting many months longer. The ever-present fear in the minds of the business men is the activity of the socialists and communists, and the introduction of fanciful ideas of government and finance by some of the long haired type of radicals.

So far as I can learn, there are no figures available from which to judge of the success of the conversion loan which is now being floated and on which subscriptions close early in September. They all speak hopefully, but with some reservations. The general attitude is that the people will not subscribe until the last days. My rough impression is that the maturities are now being comfortably taken care of, but that the subscriptions are only about 50% of expectations.

There are about 55,000,000,000 to 58,000,000,000 francs of bonds de defense outstanding, maturing, of course, every day. They are issued for one month, three months, six months and one year. Some days they are short and some days they are over in subscriptions to take care of maturities, but the average recently has been pretty good. Some fear is expressed that if they have a failure of the present loan, it will mean an enforced conversion of the bonds de defense and a very severe blow to French credit. The only other resort, if conversions are not effected and maturities cannot be met, is inflation by further issues of Bank of France notes, of which they have had all that they want and more.

You know the new bond is a perpetual 4% rente, issued at par in exchange for bonds de defense, with all of the exemptions and privileges attaching to the existing issues, and with the obligation of the Government to pay interest on the basis of the sterling value of the franc figured over an average period each day, at the rate of 95 francs to the pound. Of course any distrust of the

Paris, France
8.19.25

Mr. Winston

franc which caused a decline in its sterling value would simply add to the budget burden in paying interest on these new rentes. I have never fancied the scheme myself, but am led to believe that the emergency justified some such radical scheme.

Of course you have heard the many rumors of the resignation of Governor Robineau following the disclosure of irregularities in the accounts of the Bank. I am told that twice he submitted his resignation, which quite likely would have been accepted had they been able to find a successor. Rumor has it that the job was offered to Monsieur Sargent, who was at one time sous-Governor of the Bank, later an officer of the Treasury, and at present the head of one of the banks in Paris. I am told he declined. And the same story is generally heard as to Monsieur Joseph Simon, head of the Societe Generale, to whom I gave you a note of introduction.

I have just had luncheon with Monsieur Simon, and had a long and confidential talk with him. He tells me that he is now of the impression that there will be no change in the governorship of the Bank, at any rate for the present.

I went through a considerable part of the Bank of France yesterday, - the first time that I have made a tour of the premises in about nine years, - and was astonished to find the improvements which had been made since Monsieur Pallain resigned. It is really a modern, up-to-date institution, so far as one could judge by the way the work was being done. It is fully equipped with American tabulating, adding and type machines, and with all the modern appliances for accounting records, etc. The dingy old building has been repainted and refurnished with modern furniture; the girls have all been put into so-called over-alls, and it has a very neat, businesslike appearance. I also visited the new branch they have established out near the Etoile and I do not believe we have anything any better for any bank in the United States. At least all of this is to the credit of Monsieur Robineau, who is very much beloved and trusted by the staff of the Bank, even though he may be a rather weak man in combatting importunate politicians. If Robineau has some part of the blame for juggling the accounts, I certainly feel that the regents of the bank have more. And when his own people appeal to him on the ground of patriotism, of course the difficulty of his position is obvious. Nevertheless, a stronger man would have resigned and precipitated a crisis, however great it had been. That, I am told, is the argument used with all of them, - that it might have disrupted French finances and turned them inside out consequently.

I would like to give you some detailed account of my talk with Monsieur Simon:

His history is briefly this: As long ago as 1906, he was Chef de Bureau to Caillaux when he was in the Cabinet; has known him all his life; and has a very high regard for him as a man of culture and ability. He says he comes of an excellent family, and while under a cloud, he, nevertheless, is the strongest man in France in monetary and financial matters, but, of course, not as strong politically as others.

Much of what I am writing may already be known to you, but I will burden you with repetition:

The present understanding is that Caillaux will head a mission to the United States which is proposing to sail not later than the fifteenth of September. Simon has urged that the mission sail as early as possible, and fixed September 15 as the latest feasible date. He is to be a member of the commission himself, and he tells me Caillaux is determined to select some of the leaders of the various

Paris, France
8.19.25

Mr. Winston

(3)

political parties as members of the mission, as only by that means will it be possible for him to deal with the parliamentary situation which will likely arise on his return if a settlement is effected, as it will need ratification by the parliament and only by having some of the important men of the various parties committed to the settlement can he get ratification. I think Simon feels, - and possibly Caillaux - that such a mission is justified by the complexion of our own debt funding commission, which contains representatives of the two political parties in Congress.

The French mission plans to go immediately to Washington on landing in New York, without seeing anyone, believing that courtesy demands this. Simon himself seemed to be a bit uneasy about the uncertainty of the political situation at home, in a general way feeling that an arrangement of the American debt is but one step in a whole series of reforms in finance and monetary matters which should take two or three years to accomplish under the continuous management of the same men. And under their system of government, they can hardly expect the present cabinet to last for any such period, and consequently the policy of continuity will be difficult to carry out.

He has asked me some questions about the personnel of the Commission, which I have answered with a good deal of caution, telling him something of who the men are, and what their history has been; explaining that Mr. Mellon is a man of great skill, who deals with facts and not illusions, and that it would be a very wise thing for them to take to America, complete as possible, information about their situation, and in such form that it will give Mr. Mellon a thorough understanding of their problems.

I asked him if there was any basis for the uneasiness about the promptness with which the French Government was paying its current bills; and if there was none, that should be dispelled; but if there was any foundation for it, this should be disclosed, as well as all other material facts bearing on their capacity to deal with their financial problems.

He said that on the whole he felt that the Belgian settlement, if correctly reported in this morning's newspapers, would be helpful, the principal and most important thing being the apparent disposition of the American Commission to deal with the problem of payment upon the basis of capacity, rather than upon the amount of the obligations per se.

He thinks that the budget situation is showing a constant improvement, the current year's deficit of 2,000,000,000 francs being a great improvement over former years. And he was hopeful that in the near future a balance can be struck, but he urged all of the difficulties which we have all heard repeatedly about direct taxes, the difficulty of getting adequate taxes from the farm classes, etc.

One of the great difficulties they are facing is the uneasiness of the public generally about political conditions, and their fear of a socialistic government. The peasant classes in France are mostly small agriculturists, as you know; that is to say, property owners and savers. The classes having socialistic tendencies are wage earners and a considerable section of the so-called intellectuals, - professors, lawyers, and the like. These latter classes are active and aggressive, while the farmpeasant is a quiet fellow, who stays at home and works hard on his farm, saves his money, hates to pay taxes, and gets frightened at the idea that his property may be taken away from him.

Simon points out that the collection of the taxes now imposed is being made most effective. He says that in a big bank like the Societe Generale, with branches in so many towns, they have a good chance to observe this. He thinks the reports of failure to collect taxes are grossly exaggerated and most unjust.

The income tax is not as productive as it should be, but he calls attention to the fact that this is a new tax, only imposed since the war; that the people are not accustomed to it; that it is abhorrent to their traditions and temperament; and that its development will necessarily be gradual. Even so, when one considers that most of the income from securities is already taxed up to 25%, such as coupons and dividends, and the income tax is imposed on top of that tax, the actual figures as to direct taxation are a bit misleading. Increases in the return from the income tax will not be by an increase of rate, but rather by spreading the area of the tax over greater numbers.

I asked him whether he thought the reduction of the bank rate to 6% and, in general, the maintenance of present rates on the government's borrowings was a wise program; whether rates should not be increased, some pressure put on credit generally, and the short time securities of the Treasury put on a more businesslike basis as to the value of funds. He said that that criticism they had had many times; that the Treasury consulted the principal bankers as to whether the rate should be raised, and they were unanimously against it, all of them stating that an increase in rate would be regarded by the holders generally of the bonds de defense as evidence that there was something wrong, and that it would actually have the effect of frightening holders and reducing subscriptions rather than the reverse.

Of course you realize that Simon is non-political, and one of the thoroughly sound, able bankers of France. He agreed with me that the ideal program would be, first, to complete some kind of a security pact and give a sense of confidence as to political conditions in middle Europe; then to fund the American debt; and, following that, undertake a vigorous monetary and fiscal reform, which would include revaluing the franc and revising the Government's debt, if possible with some advantage in interest. He thought that with confidence restored a good deal could be saved in interest, but the difficulty, again, was political.

The question of capacity, I think, must be preeminent in their minds just now, and he looks at that question in a fairly reasonable and businesslike way. He says that he can understand that payment out of German reparations might be objectionable in America as tending to create the impression that we would become involved in all the disputes over German reparation payments, and, ultimately, with the political discord with which this is all associated. On the other hand, we are a creditor of France, which has a certain limit to its capacity to pay its debts, that limit being influenced by the extent to which she is able to collect from her own debtor, - Germany.

I gather that he felt that a definite scheme of fixed payment over a period of years might, on the one hand, have the effect of imposing too heavy a burden, or, on the other hand, might call upon France to pay less than perhaps possible if Germany were able to carry out the Dawes Plan in a larger way than many people now suppose is possible.

I know nothing of what is in their minds in the way of a proposal, but should suppose that in some way they would hope to have ~~something~~ greater or less according as they get more or less from Germany. It will be the same old difficulty, which I should hope, however, could be dealt with so that a contract can be effected.

I gained the impression that Caillaux is going to America with the intention of getting a settlement if it is possible to do so. He may not have an acceptable proposal, but he will certainly have some proposal which he will be prepared to fight for with his own parliament on his return if it can be put into a shape acceptable to us.

My own belief is that almost any settlement is better than a break just now, especially as Simon tells me that the country is in a mood now to make sacrifices in order to put the house in order.

With a commission such as Caillaux has suggested, I can well imagine that you will be indulged with a good deal of oratory. After a good many years experience with these folks, my suggestion would be that the oratory be allowed to flow just as freely as possible; that the members of our own commission do not attempt to deal with the members of the French commission by argument, expostulation, or admonition. If they could listen patiently to these gentlemen, exchange patriotic speeches without limit, and then let Messrs. Mellon and Caillaux sit down privately and arrange the deal, it will be found much easier to let Monsieur Caillaux convince his own people, and Mr. Mellon our people. And the effective thing to be accomplished by the commissions will be the votes among themselves whether they will agree to the proposals of the respective chairmen or not. I can assure you that it will be very much easier for Monsieur Caillaux to convince his own colleagues than it will be for our Commission to do so.

There is one point which I promised Monsieur Simon to speak to you about very confidentially.

He says that it would be a matter of much delicacy for him to seek the advice of any of his American friends while he is negotiating with the Commission, on which matter I think he is quite correct. I told him I would speak to you, however, about the possibility of some private discussions of that character in case he felt that he needed the advice of some reliable American friends while he is in Washington. It would be a very excellent thing if that is done. And you know of a similar case where the results were good.

I had hoped to visit Paris without being under the necessity of seeing Caillaux, fearing lest it might cause some embarrassment. But when I was at the Bank yesterday, Robineau told me that Caillaux knew I was here and would feel that I had been discourteous if I did not call to see him. I explained to Robineau that my colleague in Paris was the Governor of the Bank of France; that I was not official in any way; and did not want to make any calls which might be misinterpreted. He said that that would be carefully explained to the Finance Minister, but he strongly urged me to see him. So I am going to have a talk with him late tomorrow afternoon after having another visit with Robineau. Of course you know the way things flash around here in Paris. While Simon only reached Paris this morning from the country, he had already been advised of my appointment with Caillaux, and wanted to know whether I proposed to see him alone, or would have anyone with me. I think he was afraid there would be someone with me.

While my talk with Caillaux may lead to some modification of what I gathered from Simon, at present my feeling is that the French are earnestly desirous of settling the debt; are probably encouraged to feel that they can as the result of the Belgian settlement; will undoubtedly need to go through a period of discussion and bargaining; will probably have a great variety of things to suggest; but, in the end, if we are reasonably generous, we should be able to get a settlement; and any settlement is better than none. So I hope that Mr. Mellon and Monsieur Caillaux

Paris, France
8.19.25

Mr. Winston

(6)

it all up without a lot of wrangling in the commission, which would endanger
result.

I will continue this letter at the first opportunity after seeing
Monsieur Caillaux, but, as I am leaving for Switzerland tomorrow afternoon, I may
not have a chance to fix it up until next week.

One impression I got from the bankers is the probable urgent need of a
moratorium with the French even greater than with the Belgians. They do need a
period after the uncertainty of the debt obligation is disposed of within which to
carry out the rest of their financial and monetary program, especially to get the
budget balanced. And for the first time I get the impression that the effort to
put the budget in order is a serious one with some chance for success.

Continued - August 24, 1925.

As stated above, I had a long visit at the Bank of France last Thursday
afternoon and went directly from there to make my call on Caillaux.

On the whole he impressed me quite favorably. He seemed to be a man of
culture and energy, but not afflicted with the French nervousness and excitability.
He speaks English very well indeed. Fortunately he caused me no embarrassment by
attempting discussion of debt negotiations, or making any special requests for as-
sistance, or loans, or anything of that sort.

He was anxious to tell me something of his program, which I can describe
in a few words:

As to the budget, he says that he can accomplish balancing it, assuming
that an arrangement is made as to the British and American debts, and is within strik-
ing distance of it now. He had the figures all on his desk, which he said he would
have been glad to show me had there been time, giving the various changes proposed
for taxation.

Among other things, he says that the maximum inheritance taxes will go
up to about 80%, and the maximum income taxes in the high brackets he proposes to
go as high as 70%. And other sources of revenue are to be tapped. He complained
a good deal about the French system of taxation, - the product of many years' ex-
perimentation and efforts on the part of the Government to meet a characteristic
French demand that the collection of taxes shall be reduced to a mathematically
exact calculation of how the burden shall rest with justice to every tax payer. He
said it would be better for France if they had a simpler system and more direct taxes,
but the French temperament would not stand it. He explained that the direct income
tax was new since the war, and he agreed that to be more productive it would need to be
spread over a wider area; and that simple increases in rates were dangerous in
developing various expedients for escaping taxes and driving money out of the country.

He claimed that it was too early to gain any idea of the success of the
pending loan, which had encountered difficulties because of the harvests, which oc-
cupied the peasants, and because of the strike of the bank clerks, which made the
work of the banks ineffective; also because the old Bonds de Defence paid 1% more
than the new loan; that there was no advantage in conferring before the last days,
and consequently results could only be expected late. Subscriptions were scheduled

to close September 5, but they are being extended, probably until the end of September.

He spoke of the prevalent opinion abroad that the French were not paying adequate taxes, and asked for some expression about that. I told him I did not think that all the people of America could be convinced about that one way or another by a detailed explanation of the complicated system of taxation in France. The only argument which would be convincing would be a balanced budget, and once that was done the criticism would disappear.

He was very positive in his assertion that with a balanced budget he would propose to deal with the floating debt vigorously, and ultimately effect a consolidation of the debt. And, with a reasonable situation as to the debt, they must effect a stabilization of the franc for a period and then revalue it at some figure to be determined. The alternatives to a successful consolidation of the debt by some such measure as that being attempted now would be either further inflation as the maturities were taken care of, by note issues by the Bank of France, or else a forced conversion, which would hurt their credit. I believe at first Caillaux was supposed to favor an enforced conversion, but the bankers talked him out of it, stating that it would wreck the country. He is supposed to lean somewhat to that and somewhat to capital taxes.

He thought the French people would accept a revaluation of the franc if it did not involve a reduction in the amount of paper money in circulation.

Then he wanted to know in a general way what the American attitude was and whether, in case of need, they could turn to the United States for help in their program. I told him that if he had in mind some specific transaction, such as a loan, the past record in that respect indicated that the American attitude was helpful. He must bear in mind, however, that while the Federal Reserve System had a certain control of the use of its own credit, that was a very small matter compared to the attitude in general of American investors, which could not be controlled. But during the last two years we had loaned \$2,000,000,000 to the rest of the world by absorbing security issues, and some further sum in the way of bank loans and credits. If anything developed to shake American confidence in European affairs and that investment market closed, it would add very seriously to their difficulties; that foreign investments were new to Americans; and that they were still timid about them.

He wanted more information about this, and I explained how successively Switzerland, Holland, England, and then France had suffered from a shock to confidence. The case of Switzerland being typical, where the proposal for a capital levy resulting in a flight of Suisse francs, and temporarily wiped out the balances of the Bank of Issue, which had to supply the exchange to timid Suisse people.

Not much developed in the talk beyond giving me the impression that he was a pretty vigorous person and really determined to do a good job if he is given opportunity.

From various other sources I get the following information and impressions: First about the loan. I am told that it is a fact that so far the loan has been a complete failure. The Government has outstanding from 55,000,000,000 to 58,000,000,000 of short paper, of which about 15,000,000,000 is held by the banks

Paris, France,
8.24.25

Mr. Winston

(8)

40,000,000,000 by the public generally. It is the 40,000,000,000 with which we must deal. Outside of the City of Paris, I am told, subscriptions last week amounted to only 1,000,000,000 francs. It was at first hoped that they would get at least 20,000,000,000 converted. They are now talking about 10,000,000,000 being a successful result (when it would, in fact, be a failure and leave them in a difficult situation).

That this is beginning to be appreciated would appear from a statement made to me yesterday by one of the special American Newspaper Correspondents, that there were stories about that they were again having difficulty in France in meeting maturities and that while the statement of the Bank of France showed that they had a good margin on their note issue, if the true facts were known it would be shown that the new limit had already been exceeded by 2,500,000,000 francs. I, personally, don't think that story is true. But it indicates the degree of nervousness which exists.

There also are stories around that the fighting in Morocco is costing them vast sums of money beyond what they have stated, and that they have fixed up some deal with the Spaniards to finance it so that it does not show in the French figures.

There is a good deal of discussion and uncertainty about the commission to go to Washington. The last time I saw Simon, he asked me whether the commission should all go at the same time, or whether he, Simon, should go ahead of Caillaux. I told him I thought that was the sort of question which should be dealt with by private inquiries at Washington. Then he wanted my personal opinion, and I told him I would like time to think it over, but my first impression was that Caillaux should go at once himself. It would add dignity to the proceedings; would give the commission an appearance of responsibility which it could not otherwise have, and avoid the unfortunate impression resulting from Parmentier's visit.

Subsequent inquiry leads me to believe that Caillaux's position is a very difficult one. The socialists are in position to unhorse this Government at any moment. They know that if they do so the burden of dealing with the Moroccan situation and with these debt negotiations will fall upon them. They prefer to sit by in the position of vetoing or approving procedures, rather than assuming the responsibility of initiating them and conducting them. Caillaux, accordingly, is anxious to make no effort at funding the debts which is unsuccessful. And I think his disposition might be to send Simon on ahead to spy out the land, and, if there is hope of success, then to go over and finish up, himself, but, if not, to escape the odium of failure by not going.

The rumor reaches me ^{that} an unofficial proposal for a 99 year system of payment, with 2% interest, has been transmitted and rejected at home.

Now there is no doubt that the first reaction to the Belgian settlement here was rather favorable, as it gave the impression that capacity was going to be an important consideration in fixing the amount. Since the figures have come over they have been analyzed pretty carefully here, and the French now seem to draw the conclusion that the amount to be paid by the Belgians, increased to the proportions of the French debt, and without the special concessions made to Belgium as to the pre-armistice debt and interest, etc., will put an unsupportable burden upon the French and that they could not pay that amount. The statement that the terms accorded Belgium were of a special character out of respect to some moral obligation

created by President Wilson, has given them a chill. Possibly it is just as well that this should be so if the Funding Commission is ready to make some concessions to the French when they come to negotiate.

The facts are, undoubtedly, that the burden of the foreign debt on the French is much heavier, proportionately, than the burden of the foreign debt on the Belgians. The Belgian foreign debt amounts to about \$80. per capita, or thereabouts, and the French foreign debt is possibly \$100. per capita. Belgium, of course, suffered little devastation compared to France, and had priorities in reparation payments which has put them in a fairly strong position. The French, having to pay the reconstruction bills themselves, without adequate reimbursement from Germany, have gotten their finances in a very bad state.

Of course we must remember at home that the whole scale of living here is almost poverty along side of our scale of living at home and has a connection with the difficulty of collecting taxes and the meagre investment fund available for dealing with their domestic debt, compared with some other countries. For instance, a friend of mine has just rented a large house under an arrangement by which he takes over the chef and butler. The wages of those two men aggregate less than 500 francs a month -- one of them gets the equivalent of \$10.00, and the other \$12.00 a month. Parmentier tells me that his apartment is run by a frenchman and his wife. He has had to increase their wages two or three times recently to meet the added cost of living, and he says he now pays them 525 francs a month. They do all the work in his apartment and the man, in addition, takes care of his car. If this scale of living is applied throughout France to all classes, one recognizes what a slender margin there must be for taxation and for investment.

Up to this point I have been rambling along, recounting conversations and impressions as we would in discussion. Now for a few specific conclusions as I see the picture here:

1. The domestic debt of France is some 300,000,000,000 francs. Of this 55,000,000,000 are short obligations maturing every day. These are a menace to the nation, and with any shock to confidence, the only way in which they can be paid is by inflating the currency.

2. Caillaux's effort to deal with this was the result of a choice of the following measures:

- a. a capital levy
- b. an enforced conversion
- c. a further inflation of the bank note issues
- d. an obligation issued on a gold basis.

He selected the fourth, fixing the rate at 95 francs to the pound, and the interest at 4%. The result of the loan, so far, has been a complete failure. No one knows what the reaction will be when it becomes publicly known, and the date is being deferred in the hope that something will save the loan.

3. The Bank of France has, in part, lost control of the situation. Its commercial portfolio is of negligible amount. Most of its bills are simply collection bills discounted for five days. The bulk of its earning assets are the direct obligation of the Government. There is now no hope of the Government repaying. Consequently no bank rate is effective. And the bank has lost control of the possibilities of inflation due to issues of notes made on Government account.

4. The budget has not yet been balanced. They admit a deficiency of 1,000,000,000 francs. It may, indeed, be larger than that.
5. With this situation at home, they are commanded by both the British and Americans to fund their debts. I think it has given them a tremendous shake-up. There are some in France, and I believe influential people, who feel that the situation is rather desperate, and that the heroic measure would be to frankly tell the British and American Governments that they cannot and will not pay; make the sacrifice to their credit; and then do their best for their domestic creditors.
6. The present painleve government is retained in office by sufferance of the socialists. When parliament meets they may go out. It depends upon the outcome of the debt negotiations, the Riff war and the pact negotiations. If they go out, there is likelihood of a socialist government under Herriot, or the like, and all sorts of fanciful attempts to deal with the debts and like matters, probably including a forced conversion and capital levy, all calculated to scare the French investor out of his wits.
with
7. There is, nevertheless, the feeling that/the suspension of reconstruction work (which I believe is almost complete) the prospect of collections from Germany, and a pretty good domestic business situation with an improved balance of foreign payments, if they can make a liberal adjustment of foreign debts, they can some way or other wiggle out of the situation.
8. It is probably true that if the franc can be stabilized and the budget balanced, even though the domestic debt is not reduced, the thrift and industry of the French people will result, within a few years, in the accumulation of a savings fund which will constantly lighten the burden of the debt.
9. With this outlook, while they were pleased at the evidence of a generous attitude towards Belgium, they are disturbed by the statement that it was a special arrangement for Belgium which will not apply to others. Roughly, if the French debt is three-quarters of the British debt, then the French payments will be three-quarters of the British payments, or \$120,000,000 a year. This would be beyond their capacity, especially as they must make a funding arrangement with the British as well, and the British seem to be advertising strongly the opinion that the French are capable of making very considerable payments.
10. I gather that the Belgian schedule of payments starts at about \$4,000,000, and, after ten or twelve years, reaches nearly \$13,000,000. Against this there will be still some payments by Germany which will be applicable to the payment of the debt, so that the pressure on Belgium will be much lighter. Their work of reconstruction is completed. They have the benefit of priorities in reparation payments from Germany, and they have been forgiven a large part of their foreign debts. France, on the other hand, had no preference from Germany, had enormous reconstruction projects to finance in northern France, has had but small contributions of cash from Germany which will be applicable to finance reconstruction, and will need a considerable part of whatever Germany can pay hereafter for the improvement of her domestic national debt situation.
11. Finally, I think it is a fact that if debt negotiations fail, and, at the same time there is a loan failure in France, they will be driven pos-

Paris, France
8.24.25

Mr. Winston

(11)

sible an enforced conversion of the domestic debt; the domestic credit of the Government will suffer tremendously; and there will probably be some flight of capital, with the resultant pressure on the franc.

12. But there are, of course, offsetting considerations, one being the fact that the inflation which has taken place in France has reduced the burden of the debt to very much less than its nominal figure. If the French were as complacent about paying taxes as the Anglo Saxons, the burden of the debt would be much less, but the psychological limit of taxation in France is low, - much lower than in either England or America, and the same rules which would apply to a British adjustment will not apply to a French adjustment because we are dealing with Frenchmen and not Englishmen.

My best judgment is that some kind of settlement must be made with the French if they are to avoid trouble; and that if these negotiations fail trouble is almost certain to come.

I have had quite a few talks with Morrow, and with Gilbert, as well as some others, to get the impressions they have gathered from talks here. I think Morrow's idea is that the French can pay a total of \$100,000,000 a year to the British and Americans together. But, of course, with us this would include the \$20,000,000 they are now paying as the interest on the debt for the sale of supplies. The British, on the other hand, seem willing to accept a more moderate fixed obligation, and take a part of their payment conditioned upon German reparation payments.

My own feeling is that the best prospect of collecting from France lies in very moderate payments indeed for the first period of, say two or three years, giving them a chance to put their domestic situation in shape, and that after a few years their capacity to make foreign payments will be very greatly increased if they escape the present crisis.

Another thing of which I am convinced is that a reorganization of their monetary situation is essential to a continuance of foreign payments. This is because of the menace of their floating debt. If they undertake to pay us considerable fixed sums, and close to the margin of safety, and then they have any difficulty with their domestic debt at all, their only recourse is to the Bank of France, and that means depreciation of the franc and of the exchange.

I may write you something more later, especially after we learn more of the negotiations in London. But I will let it go for the present, as Dr. Stewart is leaving tomorrow and will take it to you.

Sincerely yours,

Honorable Garrard B. Winston,
Under Secretary of the Treasury,
Washington, D. C.

FEDERAL RESERVE BANK
OF NEW YORK

Hotel Majestic,
Paris, France,
August 24, 1925.

Dear Mr. Case:

This is to give you some account of our trip to Switzerland.

I arranged to meet the officers of the Bank at Bale on Friday morning, but it seems that they were scattered in various places and were unable to get there until the afternoon.

We met at their agency at 4:30 o'clock, and it developed, as I feared, that the meeting was more or less of a function, and we were regarded as personages. On that account the conference was not as productive of results as Dr. Stewart and I had hoped it would be.

The bank, as you know, is a comparatively new one, - seventeen years old; is run by three managers, Messrs. Bachmann, Schnyder and Weber. They have a Board of Directors, which has a President, Mr. Ustersi, and a Vice President, Mr. Sarasin. Mr. Usteri is an old man of eighty, formerly a senator, and a man of very high standing in Switzerland. He, unfortunately, speaks no English, being the only one there who did not. I think he takes himself rather seriously, is jealous of his position, and, unfortunately, started the meeting by reading a speech, which then had to be read in translation. Thereafter every single word spoken had to be translated for his benefit, although everyone else in the room understood.

Mr. Sarasin, the Vice President of the Board of Directors, is the head of the banking house of that name, closely allied by blood and marriage with the Iselins, and one of the foremost men in Switzerland. He speaks English perfectly, and is a man of great intelligence and ability.

Mr. Bachmann impressed us favorably. He is a man of intelligence and knowledge.

Mr. Schnyder is a great talker, and a man of little consequence.

And Mr. Weber we did not get much from, though what we did was favorable.

Unfortunately there was no opportunity at that meeting, nor at dinner that night, nor, in fact, after dinner to discuss the details of our account. All of the officers of the Bank understood the embarrassment and difficulty because of Mr. Ustersi's presence. And Mr. Weber, after dinner, said that he had wanted to discuss these matters, but that it had not proved to be possible. So he asked if I would be good enough to write them, which I shall do after my return to New York.

What developed from our conversation was interesting in disclosing the fact that Switzerland is now in the throes of the same difficulty that some of the other countries have been over here which have reestablished their currency on a stable basis; and that is their being flooded with gold. It has resulted in the Bank's portfolio being pretty well liquidated. Their domestic portfolio is so small that it gives them no hold on the credit situation, and furnishes insufficient earnings. They have accumulated large foreign balances, principally in New York and London, but in other countries as well, which they are using by buying bills and short-time governments, these making their principal earnings.

A couple of years ago they endeavored to reduce their gold by putting it into circulation; and did pay out 160,000,000 francs in minted gold. Of this about 30,000,000 francs came back to the Bank, and about 130,000,000 francs was hoarded by peasants who got frightened at the socialist proposal for a capital levy.

Private money in Switzerland is today loaning at about 2%. The Bank rate is 4%.

They tell me that while some of their foreign trade, such as the exportation of ribbons and watches, has suffered somewhat, nevertheless business conditions in Switzerland are pretty good. And the travel crop this year has been excellent. The exchanges are running strongly in their favor, and Mr. Sarasin estimated that every year the Suisse had about 200,000,000 francs to invest abroad.

As you know, the Government recently repaid its loan of \$20,000,000 which matured on August 1 in America. This has been done without recourse to the Suisse market. And the Suisse Bank sold 30,000,000 marks of gold to the Reichsbank while we were in Germany, offering 60,000,000 more if the Reichsbank cared to take it, which they did not. Gold is coming to them from Scandinavia, and from Holland. With their government finances now in good condition, and with the balance of trade in their favor, with the Bank's portfolio pretty well liquidated and the Bank rate ineffective, they are naturally disturbed at the influx of gold because the Bank's circulation is now between three and four times the amount which it was prior to the war. They have a reserve of 65%.

We talked a good deal about central bank cooperation and the possibility of the gold exchange standard having the effect of causing involuntary inflation in the gold standard countries. This caused some significant looks about the room, and I think they have a little guilty feeling that we consider Switzerland one of the offenders. I explained to them that in an immense market like ours, the small amount that they were investing was not of great consequence, and we had felt that they had been willing to earmark gold pretty freely, were glad they had done so, and hoped that they would continue to do so.

There was also a good deal of discussion about the outlook of Suisse finances generally. Mr. Sarasin stated that in his opinion Switzerland could be expected to repay all their foreign loans, as they had the loan maturing August 1; that some part might be refunded but he thought it unlikely; that the Suisse were definitely now in the position of a lending nation. Of course it is significant with this the case that they employ as much of their balances as they do in America, where rates are comparatively low as against continental Europe. I imagine their confidence in our gold standard has much to do with it, as well as their confidence in the Federal Reserve Bank.

They were all greatly pleased and complimented by our visit, and expressed a strong desire to take part in any program undertaken at our initiative, or as they expressed it, under our leadership. I explained to them that while it was true that we had the resources and were sympathetic to the idea of a general monetary reconstruction in Europe, it must not be understood that we were seeking leadership; we were not sufficiently informed of European conditions to undertake that role; that monetary reform should be undertaken in Europe under their own leadership; but that we were glad to listen to proposals and help if it seemed feasible to do so. We carefully explained that the terms of the Genoa Resolutions were not, in our opinion, appropriate to the present situation, especially in the suggestion that there would be competition for gold when monetary reform was seriously undertaken. Besides that, we were strongly of the opinion that nothing in the way of a formal conference between banks of issue would prove to be feasible, as they would always be influenced by the necessity for a central bank to give consideration to local problems, in preference to international problems; and that each central bank should be entirely free to do so; but that, where there was no conflict with domestic interests, they should endeavor to cooperate. And the first step was to cultivate personal acquaintance and confidence, and that that was one of the principal objects of my visit to Europe. Mr. Sarasin and Mr. Bachmann were both of the opinion that that was the right way to progress, and that anything like formal meetings should be deferred for a time until we had better private understandings among ourselves.

They displayed some concern about the activities of the socialist and communist parties in Europe, especially at the present time in France. Switzerland is surrounded on all frontiers by countries which have suffered so severely from the war that the reactions in Switzerland seem to cause them dismay. They seem to act as a clearing house for advanced notions. There is an active socialist party in Switzerland itself, and, just now, they are watching with some apprehension the activity of that party in France.

There is nothing like a discount market in Switzerland. There is a certain amount of trading in bills between the banks in the cities of Zurich, Berne and Bale. But Switzerland, they claim, is over-supplied with banks. They have nearly 800. Competition is pretty keen and there is little need just now to use the bank of issue.

Mr. Sarasin said he thought the role Switzerland would play for some years would be that of a small money lender to the rest of the world, the Suisse people taking a moderate amount of conservative investment securities, and the Suisse banks maintaining moderate portfolios of foreign bills. Their one fear, of course, is inflation.

They were interested to gather from us whether we were liable to undertake any radical measures to prevent further imports of gold. I think they were fearful lest we do so. I told them that we had so far gotten along without that and I hoped we would continue to do so; that we preferred to see this gold problem work itself out by methods of cooperation which would avoid abnormal tinkering, any efforts to change gold points, and so add to disordered conditions.

On the whole the meeting was unsatisfactory in bringing out details which we hoped to get at, but was satisfactory enough in establishing friendly and cordial relationships, and in satisfying us that they had a most tremendous confidence in America and in the Federal Reserve Banks.

Paris, France

FEDERAL RESERVE BANK OF NEW YORK.....8.24.25

Mr. Case

(4)

I described the System; its organization and its method of operation, concerning which they displayed a good deal of ignorance. The questions asked showed that they were uncertain of the feasibility of having twelve banks, each issuing its own currency and each having its own rates of discount, but a description of the way the system works in those matters seemed to completely dispell their doubts.

They were very insistent in urging that I should visit them again and spend more time with them the next time I come to Europe. They want me to spend a few days in Zurich and become acquainted with the Bank in some detail.

Mr. Usteri is visiting America shortly to attend a meeting of the Inter-Parliamentary Union. He has great pride in the prospect of meeting the President. I believe he expects to land in Canada and go to Washington by way of New York. I think he is sailing very soon, and he may even reach America before I am home, so look out for him and give him a good look at the Bank. He does not speak English, but will have someone with him to interpret.

This is about all that occurs to me to recount about our friends in Switzerland.

Sincerely yours,

Pls. Strong

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank,
33 Liberty Street, New York.

FEDERAL RESERVE BANK
OF NEW YORK

RECEIVED
Copy to G. B. W.
SEP 18 1925
J. H. C.

Hotel Majestic,
Paris, France
August 26, 1925.

Dear Mr. Case:

Some of my letters will give you a little idea of the financial situation here, but I have written nothing generally about conditions in France.

So far as the crops are concerned, on the whole they have been pretty good, except that just at harvest time they had some heavy rains and I hear that there has been quite a little loss as the result. No exact estimates are available, but the crop is regarded, generally, as being better than last year's. The principal losses due to bad weather have been in the vegetables, the late grains, and the fruits.

I have now been over the lines from Brussels to Paris, Paris to Biarritz, and Paris to Bale, these being three of the important lines. And I am not at all impressed by their physical condition. In the last thirty days they have had twenty accidents to passenger trains, some of them very serious. Most of them have been due to the trains jumping the tracks. They all run at high speed, and I think too fast for the condition of the lines.

Friends who have been motoring throughout France tell me that the roads are also in bad repair.

We visited Versailles the other day, and there the palace is undergoing repairs, entirely due to the generosity of Mr. Rockefeller. But the grounds are not kept and it is a rather sad spectacle. This is true, I am told of the Louvre. That building needs constant attention but is not having it.

These evidences of national economy are indicative of the straights the Government has been placed in by their budget shortage and the difficulty with the floating debt.

I have had little chance to see anything of the devastated areas, but am told that reconstruction work is completed as to the farm lands, public buildings, many of the churches and important business and industrial plants. But there are a good many private dwellings still to be rebuilt or repaired, though I gather that the owners have accommodated themselves to conditions.

The nation is certainly at work, however. I hear there is practically no unemployment of consequence, and the visible figures of the balance of trade continue favorable. One must, however, make allowance for these figures in one respect, which is not commonly known. France and her colonies, particularly French Indo-China, are regarded as being under one monetary system, and partly for that reason all French exports to her own colonies appear in the figures of exports, although they do not produce a true balance of payments. Of course the exports of the colonies to the rest of the world are not included for some strange reason.

Inasmuch as the exports of France to Indo-China and other colonies are heavy, but result in payments to France in her own currency, the effect is somewhat to swell what appears to be a favorable balance of trade, without, however, giving the foreign exchange needed to protect the franc.

Just now there is something of a crisis in the wine business, especially in the southern part of France, and pretty heavy losses are expected.

All of my talks with Frenchmen indicate that outside of the agricultural classes they are feeling the burden of taxes pretty heavily. My friend Baron de Neuflyze, father of the Jacques de Neuflyze whom you know, told me at lunch the other day that he paid 60% of his income in taxes to the Government. And I understand that their system of taxation is such that business losses (that is capital losses) are not capable of deduction from current income, the same as ours, and, consequently, many firms and businesses are obliged to amortize losses over a period of years.

There is also universal agreement that the general standard of living has been much reduced. French people who live in the provinces, in former years, were accustomed to spend a portion of each year in Paris, to attend the opera, do their shopping, and visit friends. They are no longer able to pay the hotel rates, nor the prices charged at the best restaurants, so they don't come to Paris. But the flood of European travel which has reached hitherto unknown proportions has kept Paris fairly prosperous.

A curious situation has resulted from the immense deliveries of reparation coal by Germany. Coming as it does with enlarged use of oil and hydro-electric power, there has been an immense accumulation of surplus coal, and the coal business is withering. Notwithstanding this, hydro-electrical development is going on all over France, Germany, Switzerland and Italy. The Suisse, for instance, include in their export figures "receipts from power transmitted over their borders," which is now considerable. Railroad lines are being electrified in many directions wherever water power is accessible, and, in time, I have no doubt a large part of the main lines of the French railways will be operated by electricity, just as a considerable part of the Suisse lines now are. It presents a gloomy outlook for the coal business, and for the extent to which reparation payments in that form can indefinitely continue.

There are some evidences of an upward move of wages, and if it should become general, I can see prospects of considerable difficulty with the circulation. The postal clerks struck for pay increases and got them. Now the bank clerks are engaged in a determined strike which cannot be settled, and the newspapers report that the postal clerks are endeavoring to support them by refusing to deliver commercial mail to the banks. Any general wage increase would undoubtedly be the signal for some price increases in the provinces, which have not yet risen to the city levels; and necessitate still further currency issues, thus still more complicating the Government's difficulties.

Dr. Stewart, I think, feels quite definitely that this development is likely, and he was interested, in discussing these matters at the Societe Generale, to hear the opinion expressed that with the franc at twenty to the dollar France would never be able to support her domestic debt; and probably would not until it got somewhere in the neighborhood of forty to the dollar. Of course this sounds like a counsel of despair, but it is not out of the question that something of that sort would develop if the pending loan is a complete failure and debt settlements cannot be effected with England and America.

My understanding is that our Government has shut down on private loans to France completely. If this should be continued, notwithstanding a failure of de negotiations, I suppose the odium of any disaster which happens over here will be promptly handed to us.

While French people are very courteous, I suspect they dislike us, and despise us for our policy.

The outlook politically is about as uncertain, unfortunately, as the outlook financially. The present Painleve Government is continued in power by the sufferance of the socialists and radicals, who are unwilling to assume the responsibility of dealing with the present difficulties, but who are always in position to vote the Government out. So it looks as though vigorous efforts were being made to smash the Riffs, put over a funding loan and settle the debts with the hope of giving the present government a new lease of life. I have heard it definitely stated that the government will go out the middle of November.

The position of the Bank of France is the outstanding illustration of the difference between our scheme of war finance and the European scheme. With the exception of the first loan of \$50,000,000, our government borrowed nothing from the Reserve Banks to finance the war, and consequently we had the obligation of a private individual or institution on every loan we made. Here a large proportion of the war borrowing from the banks of issue was made directly by the Governments. England escaped to some extent because of the decision to issue the currency notes; but nevertheless, for a long time they were burdened with ways and means advances. They have now struggled out of that situation, and their sole monetary problem of consequence is to deal with the currency notes, which they will be able to do in a year or two. Germany swept the deck clear by abandoning the old currency and reorganizing the Reichsbank. Belgium, France and Italy, however, are in the position of having their portfolios almost entirely loans to the Treasury. In Belgium, as I advised you, their private portfolio of loans and bills is only \$30,000,000, or \$35,000,000. The position of the Bank of France is similar. They have, in round figures 30,000,000,000 of loans to the Government. And their private portfolio consists roughly of 3,000,000,000 of Lombard loans to customers upon the security of railroad and other good securities, - say \$150,000,000. Their portfolio of bills discounted, of about 3,000,000,000 francs is almost entirely short bills, simply deposited with them for collection. Yesterday, for instance, the bank discounted 256,000,000 francs, and of this all but 8,000,000 francs were of five and seven day maturities, the five day bills being those payable in the cities, and the seven day bills those payable in remoter districts. This leaves the bank in a position where its discount rate is of no effect because the rate on the Government loans is a fixed rate, and the amount which they are furnishing generally to industrial and commercial concerns is too small to have a rate change operate effectively.

The Bank of France has some 200 branches and these bills are those which come from all over France. So you can see, when divided up among all of those offices, what a very small portfolio it is. It is hard to see what will be the outcome. The Government is not in position to reduce its debt to the Bank, nor will it likely be for some time, and it will be a considerably longer time dependent upon the success or failure of payments by Germany.

The striking difference between the situation in Belgium and in France

lies in the fact that the Belgian Government is willing to proceed to liquidate its obligation to the Bank assumed in connection with the retirement of the mark notes, although, under present conditions, they must do so by foreign borrowings. It will, however, put the Bank back in a position where it can become a real bank of issue and exercise a real influence through its discount rate.

Criticism of the reduction of the Bank of France rate from 7% to 6% under present conditions looses much of its force.

In a long talk with Robineau yesterday a very interesting piece of information slipped out, which I think Winston would be interested in hearing. It seems that recently a second cousin of Robineau's died and left him 1,000,000 francs in his will. After calculating the expense of administering the estate, etc., Robineau found that it would cost more to accept the legacy than to turn it right over to the State, so he relinquished it entirely.

I am told that the pressure has been sufficiently severe recently for the French Government to slow down considerably in paying their bills. What this all amounts to, I can't tell, and it may be just gossip. But I have heard it more than once.

The importance of the present situation lies in the fact that they have 22,000,000,000 or 23,000,000,000 francs of short obligations maturing before the end of the year. Nearly a half of them mature September 15, and somewhat more than half December 15, except for a negligible, scattering amount of small issues. The Bank of France now tell me that they have a margin of 4,000,000,000 on their note issue, and 6,000,000,000 on their loans to the Government. If they can whip up the present loan to a reasonably successful conclusion by the fifteenth, or have enough subscriptions accumulated by then, they may be able to take care of these maturities without asking for an increase in loans from the Bank beyond the present authorization. But I judge September 15 will disclose a good deal.

From the foregoing you may conclude that France presents the picture of a concern which is very heavily in debt; with the debt in a fairly perilous situation; with a reasonable prosperity in production of goods and in trade; but, during the period of strain, with an enforced economy which may result in an impairment of the properties and machinery of the State. If they succeed in effecting funding arrangements with Great Britain and the United States, they will then promptly need some help, and will turn to the American market. But I surmise they will also seek assistance in England as well.

My best to all at the bank.

Sincerely yours,

Reis: Strong

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank,
33 Liberty Street, New York.

London, England,
August 29, 1925.

CONFIDENTIAL:

My dear Winston:

A cable reached me yesterday just as I was leaving Paris advising me that you would like to have some word from me about the position of France.

By now you have received my letter of August 19, and I hope Mr. Case has sent you a copy of my letter of August 26 to him. I am unable to send you anything further today, but, of course, you will know that both Leffinwell and Morrow have been here. And they have seen a good many people in London and in France, and I think Mr. Morrow, at least, expects to have a talk with Mr. Mellon, and to see the President also.

You will probably discover that they have some pretty positive opinions, with which I might not necessarily agree in full. And they will also likely have some interesting information.

In the course of the next few days I am meeting some people here who are quite intimately informed about French affairs, and will be able to supplement what I have already sent.

It distressed me to gather that the American newspaper accounts of the tentative proposals between the British and French just concluded by Caillaux, were unfavorable and intimated that there were ulterior motives. I am very satisfied that no such charges are justified by the facts. It would appear to be necessary for both Caillaux and Churchill to make some reservations pending an American adjustment in order to meet possibly hostile and even critical public opinion which would be exceedingly difficult to deal with. If our people would put themselves in the position of those two negotiators over here, they would see that without such a reservation, an American settlement which differed materially one way or the other from the basis of the British settlement would arouse such hostility in either one country or the other as to possibly defeat the whole settlement. And, of course, the settlement is subject to ratification in both countries when their Parliaments meet, as I understand it.

Very confidentially, Mr. Robineau has promised me some important and confidential figures about the French position, which I believe may be very helpful to you. I think you may rely upon the figures as being accurate and a reflection of the true position. We had a very frank and friendly talk, and I explained to him frankly

London

8.29.25

Mr. Winston

2

at there was nothing which I could do in furthering these matters, except it might be through obtaining reliable facts. They should be in my hands within a week.

This is the best I can do until some time next week, when I will get off a letter in more detail.

Sincerely yours,

Honorable Garrard B. Winston,
Under Secretary of the Treasury,
Washington, D. C.

Stouey
acc

FEDERAL RESERVE BANK
OF NEW YORK

RECEIVED

SEP 5 1925

J. H. C.

Hotel Majestic,
Paris, France,
August 25, 1925.

Dear Mr. Case:

Yours of the thirteenth refers to the situation in the market, rates, etc.

It would take too long a letter to give you a picture of just how we are related to the situation over here, which is, as usual, complicated.

The gold standard countries are being more or less flooded with gold. And, to some extent, they are passing it about among themselves. The portfolios of the central banks are pretty well liquidated, and they are all more or less afraid of easy money and of inflation, and of loss of control. This has happened in London. And while I am not posted to within the last week or ten days, I have a note from Norman indicating that if matters continue as at present they will have to consider a further rate reduction.

Now my view of this is that up to a certain point we should make every effort to accommodate our policy to theirs. If they feel it necessary in meeting domestic conditions to reduce their rate, then, of course, they must do so, but should not necessarily expect us to go down with them if our domestic situation would render it perilous to do so. And, in fact, that is our situation at home. We cannot now afford a rate reduction, and the only question is whether we can afford to stay at our present level as the best we can do, or whether, notwithstanding ~~the~~ reduction in London say to 4%, it may be necessary for us to go up to 4%.

Of course you understand that the consequence of an increase in our rate, in the face of rate reductions among the gold standard countries of Europe, will be some transfers of funds to the United States by bankers generally, and by the banks of issue specifically; and that we cannot then escape further shipments of gold.

Our earning assets are now nearly \$300,000,000 above what they were a year ago, and of our earning assets over \$200,000,000 are Government holdings under the control of the committee and about \$100,000,000 are Governments not under committee control. If, therefore, we are now obliged to pursue a policy of higher rates and it does result in gold imports, the Federal Reserve System must definitely face a period of liquidation of earning assets at least equal to gold imports, and it may be that the sale of securities must be extended beyond the committee's holdings and take in some of the holdings of the individual banks.

I am hoping that there will be no important change in the situation prior to the date of the Governors Conference. At that time I shall be glad

Paris, France

FEDERAL RESERVE BANK OF NEW YORK...8.25.25...

Mr. Case

(2)

to explain to our colleagues everything that I know about the situation abroad and endeavor to induce them to a complacent state of mind about earnings during this temporary period of readjustment. If we are not successful in doing that, we are going to have a struggle with an inflation and a boom sooner or later, unless, indeed, they have an up-set in Europe which would act as a deterrent.

The letter which I have sent to Mr. Winston by Dr. Stewart's hand (and of which a copy is going to you) will, however, indicate that within the next few weeks it will likely be known whether the French will be able to meet the difficulties of their situation both financial and political or not. If they fail in doing so, I would expect to see some period of uneasiness, which might result in gold coming to America anyway. You will, of course, gather from this letter and my letter to Winston that any change in our policy must receive the most careful consideration; have full discussion; and I should hope our directors will be available when I get back for this purpose.

We are sailing on the Olympic on September 9. I would return earlier were it possible, but arrangements have been made for Vissering to come to London; I am anxious to meet the Pole there; and I also expect that Dr. Schacht will run over for a short visit; and possibly Moll of Sweden. So you see it would be inconvenient and unwise for me to leave, and the difference of a week would hardly be worth while.

I think the important thing at the moment is to keep our resources available for use in case the gold movement does again turn in our favor.

Sincerely yours,



J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank,
33 Liberty Street, New York.

London, England,
August 31, 1925.

Dear Mr. Jay:

This brief line is to comment on one or two important observations in yours of the twentieth, which just reaches me. I have read it with much interest and pleasure.

What you say about the directorium I agree to entirely. The same thing is found in every bank of issue over here, so far as I know them. It took an outsider to stir them up in the Reichsbank, - and they certainly got a good stirrer!

What I wrote about Mr. Houghton's views is, of course, exceedingly confidential. In fact the whole document is a confidential one. I am afraid our own people will not entertain the idea which we discussed, but it should be done and would lift the whole world out of a slough of despond.

The Rentenbank reorganization bill has become law, but so far they have not agreed with Mitchell on a loan, although negotiations, I believe, are still pending. Dr. Schacht is to come over to see me on Monday, and I will know more thereafter.

I really have great reservations about any prior approval by our government of the operations of the Reserve Bank abroad. It is a dangerous precedent, and heretofore we have contented ourselves with notifying them after the event.

The possibility of buying any paper from the Reichsbank, I think, is very remote; and in general I agree with your observations of its relations to the Bank of England credit. I further agree about the need for the pact negotiations being concluded first. This I told Dr. Schacht very plainly. The difference between a transactions with the Reichsbank and one with the Bank of England is that the former would simply be a temporary matter of policy and an informal arrangement, whereas the Bank of England arrangement was necessarily formal, as it was the basis of the resumption of gold payment. The need for a long commitment, therefore, was obvious, and the interest of our own country in the results (probably second only to that of the British themselves) necessitated it. Whatever we did with the Reichsbank, however, would be more in the nature of a seasonal affair with a bank which was already on a gold basis, and where we could possibly have informal understandings from time to time which would accomplish

London, England
8.31.25

Mr. Jay

(2)

everything, and more than would be possible by formal loan agreements.

But I doubt if we have occasion to do anything, especially since hearing that their divisen position is much improved.

This is all that I will bother you with just now, as I will see you not long after your return.

Thanks for your letter, and best regards.

Sincerely yours,

Pierre Jay, Esq.,
Chairman, Federal Reserve Bank,
33 Liberty Street, New York.

FEDERAL RESERVE BANK
OF NEW YORK

RECEIVED

SEP 8 1925
J. H. C.

London, England,
September 1, 1925.

Dear Mr. Case:

I am enclosing herewith for your information copy of the only memorandum I have thus far been able to prepare concerning the visit Governor Norman and I had with Mr. Mlynarski of the Bank Polski. It can be added to the others I have sent, and should, of course, also be treated confidentially.

Very truly yours,

Re: Strong

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank,
33 Liberty Street, New York.

Enc.

HAMMILL
BOND

MEETING WITH MR. F. MLYNARSKI
(Vice President, Bank Polski)
LONDON - AUGUST 31, 1925

Mr. Mlynarski was accompanied by Mr. F. A. Poklewski-Koziell, Commercial Counsellor of the Polish Legation.

State Bank:

Its capital, fully paid, is 100,000,000 zloty, of which the Government owns 1%. While the Government is authorized by law to be a stockholder, and was expected to be a large stockholder, the subscriptions were unexpectedly successful and all but 1% of the stock is held by the public. The law provides that stock may be held abroad, but there are at present no foreign stockholders. It is desired to increase the capital of the bank by selling stock abroad, but that is not at present possible.

The law requires a minimum reserve of gold and valuta of 30% of the note issue. No reserve is required on deposits. The other 70% must be internal bills. The reserve provision is the only limitation upon the note issue.

Borrowings by the Government from the Bank are permitted up to 50,000,000 zloty, all of which has been loaned to the Government for the purpose of retiring mark notes formerly in circulation.

The Bank is limited in the amount of subsidiary coinage which it may hold to 5% of the outstanding circulation.

While in Germany and Austria the bank of issue is permitted to make loans for limited amounts to the Treasury against uncollected taxes, these loans are not permitted in Poland.

Present Position of the Bank:

The Bank rate is now 10% (unless it has been increased, as is possible, to 12% within a very recent period). Its portfolio of inland bills is roughly 300,000,000 zloty. The outstanding circulation is 460,000,000 zloty, or, roughly, 15 zloty (or \$3.) per capita. The law permits the Government to issue silver coins to a maximum of 8 zloty per capita, and copper coins, 4 zloty per capita. Recently, when the bank note circulation was reduced over 100,000,000, the holdings of subsidiary coinage by the Bank became excessive; that is, over the 5% permitted. And the Bank enforced the rule of receiving payments from customers of not over 500 zloty in subsidiary coinage so as to correct the difficulty.

The circulation in Poland is so deficient in amount that the velocity of circulation is tremendous. The payment of taxes each month equals over one-third of the entire Bank monetary circulation, so that for tax payments alone the velocity is equal to four times the volume every year.

The Bank was originally organized entirely on domestic resources, both as to capital, gold reserves and foreign bills. The Polish Government loan, and the accumulation of emigrant remittances gave them a large reserve, until last January. Last year's crops, however, were a failure, and the stabilization of the currency gave it an artificially high purchasing value domestically, so that the shortage of exports and domestic extravagance in expenditures resulted in an adverse balance of payments, and a loss in the Bank's reserve until today it has in gold and foreign balances only about 40% of its note issue, notwithstanding a reduction in the note issue by over 100,000,000 zloty.

The rate of discount not being effective, credit has been rationed. And the shortage of circulation has resulted in rates for

Present Position of the Bank (continued)

The Bank of Poland exercises a practical monopoly in the foreign exchange market. Such market as there was for forward exchange has been discontinued recently since the value of the zloty declined so sharply, and the Bank has been discriminating between what it regards as legitimate demands for foreign exchange for commercial purposes, and those for simply speculative purposes.

In order to correct the adverse balance of trade, enormous increases in customs were levied commencing the middle of June. The rates were increased from two to six times the old rates. This immediately curtailed imports, as shown by the reduction from 25,000,000 zloty customs duties collected in May, to 3,500,000 zloty for the first ten days in August.

The foreign exchange monopoly by the Bank gives them command of about \$20,000,000 per annum in checks and foreign currencies, principally dollars, largely arising out of emigrant remittances. Checks are remitted for collection regularly, but currency only every two months, so that there is quite an accumulation of currency for which they do not get reimbursement promptly. Delayed remittances of currency are due to the heavy expenses and the need for making large shipments in order to get satisfactory protection and low insurance and transportation rates. The first eight months of 1924 the Bank accumulated \$14,000,000 from this source.

Under the Treaty of Versailles, Germany was obligated to take 500,000 tons per annum of coal from Upper Silesia until June 1925. Germany is the only European nation with which Poland has no commercial treaty. Commissioners went to Germany last January to negotiate a treaty, but the Poles concluded that the Germans were procrastinating with them
order to wait until the obligation to take coal had expired, so as to

Present Position of the Bank (continued)

... that as a club in the negotiations.

The Poles export, of all they send out, 40% to Germany, but import only 5% from Germany. Notwithstanding this, and being unsuccessful in the negotiation of a treaty, Poland placed an embargo on imports from Germany. They also had a dispute about exports of cattle to Germany, the veterinary examination, etc. The general impression from this narrative was that they were on bad terms with Germany, and were not using means calculated to be successful in improving their trade with them, notwithstanding their dependence upon Germany for their export market. They claim that Poland alone will consume all the Silesian coal as soon as the railroads can be turned about and extended into the east and northeast, where transportation is insufficient but where there will be a large market for coal. Railroad reconstruction means the building of about 1,000 miles of lines. But the result of their policy has been to impose a virtual prohibition upon imports from Germany. It has somewhat the appearance of sawing off the limb that represents 5% of their import trade, but which, nevertheless, may furnish support for 40% of their export trade.

The Government budget is in balance. Their domestic debt is 5 zloty per capita, and their external debt 15 zloty per capita, the latter representing principally the debt of \$178,000,000 to the United States Government, the loan of \$35,000,000 placed in New York by Dillon Read & Company bearing 8% and sold at 95, and a previous loan of about \$20,000,000 sold in New York to Americans of Polish origin, which bears 6% interest and which I believe was sold at about par.

The zloty, under the influence of the conditions described, recently declined from about 25 to the pound to about 30 to the pound, with a corresponding decline in the American market. It has now recovered

Present Position of the Bank (continued)

around 27 to the pound, partly as the result of the restriction upon imports, and partly as the result of the favorable sentiment created by the credit granted by the Federal Reserve Bank. They are fearful of a further decline due to spread of distrust of the currency, which would cause an exodus of capital. They are considering whether the Polish Government might not borrow abroad. Dillon Read & Company have an option on \$15,000,000 additional Polish bonds, but as these are now selling at 87, having been issued at 95, the outlook is not promising. (Mr. Mlynarski probably was not aware that the first Dillon Read loan was not a great success, and while \$35,000,000 was floated, only \$27,000,000 was taken, and the balance never has been sold, nor do I understand that Dillon Read are under obligation to take them).

- - - - -

In a subsequent interview with Mr. Mlynarski, he quite frankly told us in detail of the situationⁱⁿ/respect of the Dillon Read bond issue, that the entire issue did not sell and the Polish Government preferred, for various reasons, to take back the unsold portion. Since the issue was originally made, small sales have been effected, but nothing of consequence.

He also made the very important statement that the reason why the very high bank rate, the high cost of credit, and the low per capita circulation in Poland was not effective in stopping importations of foreign goods was the fact that after the currency was reorganized and stabilized, apparently foreign business concerns sent salesmen into Poland and offered large quantities of goods on credit. This caused importations in excess of the real capacity of such a poor country as Poland, and when the credits matured, the burden fell on the

national bank to furnish foreign exchange to make the payments. It

explains much of the difficulty which has now developed, and the unfortunate necessity for raising the tariffs to such a high level.

After another long interview with Governor Norman and me, he probably will decide to make some sort of proposal to Dillon Read to arrange a bank loan, secured by the Polish bonds, hoping to borrow for a couple of years until the position of the Bank is such that they can take care of the external value of the zloty without the need for using credits at all. Then, within the two year period, they would hope to sell the balance of their bond issue; that is \$7,000,000 of the original issue, plus \$15,000,000 now under option.

I explained to him that we could not grant them a credit for two years on their domestic bills, even though they were the highest possible grade.

Governor Norman's position was outlined in a letter to them some months ago in which he explained that he was opposed to granting short credits to banks of issue, but, as one of their valued correspondents, the Bank would entertain proposals for an advance of reasonable amount secured one-third by gold and two-thirds by acceptable foreign bills. Of course such an arrangement is quite impractical for the Bank of Poland.

On the whole our impression of him was very favorable as to his honesty, earnestness, and intelligence. The difficulty is, however, similar to that with all Poles, - they are not very practical people, and while they may be excellently informed, they do not know how to use their information along sound lines.

C U S T O M S R E V E N U E S

(In thousands zloty)

<u>1 9 2 5</u>	<u>With Dantzig</u>	<u>Without Dantzig</u>
January	32,300	23,500
February	26,400	24,100
March	24,600	23,500
April	36,900	24,700
May	27,600	25,200
June	26,600	21,100
July	26,800	17,600
August (1 - 10)	3,500	

August 20, 1925

Gold	121,720,412
Foreign	72,767,048
Discounts	292,849,290
Circulation	433,155,370
Deposits	71,152,385
Foreign Dep.	31,858,079

Private and
Confidential

London, England,
September 1, 1925.

My dear Garrard:

As you know, my trip so far has been entirely upon the Continent. We were in London only a couple of days before leaving for Berlin. During this period the Belgian debt settlement has been effected, the tentative arrangement has been concluded between the British and the French, and now, at the moment of writing, so far as I can gather, the French are hesitating as to the personnel of the commission to go to Washington, - whether Caillaux shall go with them, ahead of them, or after them.

As I wrote you, the Belgian settlement had a distinct reaction in France. And now I gather from the newspapers that the British-French arrangement has had a very decided reaction in America. I think I have most of the details of it fairly accurately.

On Monday I received a note from the Embassy asking if I could obtain quite a lot of information on the subject to be cabled home. And I am just now debating with myself whether it will be wise to send it in that form, or to await my return and give it to you and the Secretary personally. Mr. Houghton, in whose judgment I have a good deal of confidence, is out of the city, but it is likely that I will see him tomorrow, and I shall be guided somewhat by what he says.

In view of our relations with the Bank, and the importance attached here to the arrangement with the Federal Reserve Bank for the resumption of specie payment, it seems necessary for me to have a talk with the Chancellor. I think my failure to do so would arouse some curiosity, especially as it has been suggested to me. He, also, is out of the city, but I have accepted an invitation to motor down to his place in Kent and take lunch there on Saturday.

Of course you realize that it would be unfortunate for me to send an incomplete statement; and I believe that any statement would be incomplete until I have had opportunity to talk with both Houghton and the Chancellor.

This is the position today, and I am writing to explain it to you so that you may not think I am unmindful of your wish to get all the information available. I am also particularly anxious that neither you nor the Secretary should arrive at any conclusion as to the reasons for the particular form of the adjustment with the French and the way in which it was announced, until I have an opportunity to talk with you. I have had a very frank explanation of the matter from one in position to know the facts, and am personally satisfied that there was no ulterior purpose in the arrangement; that there was no attempt to set a trap, nor in any way embarrass Mr. Mellon or the Commission. It may be that the announcement was a bit mal-adroit.

Mr. Winston (2)

London 9.1.25.

You know, many people here interpret the Balfour note, or statement, as meaning that the British intended not only to accept no less on the loans they made than they were called upon to repay to the United States, but also to accept no more than they were required to pay. The same possibility of misunderstanding could also arise about the announcement made by the British in connection with the French negotiation. I, frankly, don't know exactly what they intend, and I am not sure that they know themselves. Certainly if they mean that they will accept both no less and no more than a payment proportionate to what is paid to us, it would have been more palatable at home than the form in which the statement did appear. But the conclusions appearing in the press I still believe are quite unwarranted and calculated to make our own negotiation much more difficult than need be.

As I shall be home at least a week before the French mission can arrive, I can explain all of this much better than is possible in a letter. And, indeed, I may decide to send something in advance of my return either through the Embassy or by mail directly to you.

With best regards, I am

Sincerely yours,

Honorable Garrard B. Winston,
Under Secretary of the Treasury,
Washington, D. C.

FEDERAL RESERVE BANK
OF NEW YORK

London, England,
September 2, 1925.

Dear Mr. Case:

Since I wrote you about the Polish matter, Colonel Logan has come to London and had a long talk with Mr. Mlynarski. They are now discussing whether it might be possible for Dillon Read to arrange some sort of a bank loan for Poland upon the security of Government bonds, with some understanding by which the entire proceeds will be deposited in the National Bank of Poland and the Polish Government maintain the account at current rates of exchange at a sufficient level to cover the credit, the idea being that this would give the National Bank the proceeds of the loan in dollars which they might use to protect the external value of the zloty.

I have explained to both Colonel Logan and Mr. Mlynarski that at the present there is no possibility of our doing more than we have already done. I have also stated that I was quite sympathetic with their desire to get assistance; that what they needed was long-time money and not short credits, and if, in a reasonable period, the Polish Government could sell an issue of bonds that would be better than any kind of bank loan or bank credits; that if any of our bankers called to inquire about a credit such as might be proposed by Dillon Read, I would be very glad to tell them what I know about the matter, without responsibility to me or to the bank. This seemed to satisfy him pretty well, although for a time he was very anxious to get some sort of credit against the pledge of some kind of security other than gold. I told him it could not be done.

As Colonel Logan will be cabling New York about this matter, you may have inquiries, and this will give you a line on how to deal with them.

I will be glad to talk with Mr. Dillon about it on my return if he wishes to drop in at the bank.

Sincerely yours,

Benj Strong
m.s.

J. H. Case, Esq.,
Deputy Governor, Federal Reserve Bank,
33 Liberty Street, New York.

Enc.

RECEIVED

SEP 12

J. H. C.

Winston

CONFIDENTIAL

S. S. Olympic,
September 11, 1925.

Dear Winston:

Of course you realize that during my visit abroad I had opportunities for discussing the whole situation as to debts, reparations, etc., with some of the best informed and most responsible people in Berlin, Paris and London, including Gilbert and the members of his organization, Mr. Houghton, our Ambassador at London, and Mr. Nelson Perkins, the American Citizen member of the Reparation Commission.

It is no exaggeration to say that all of these gentlemen, and others, are in agreement that we are in danger of making a serious mistake in these refunding arrangements if insistance develops for larger payments than can be definitely supported.

I am somewhat uncertain as to the best method of getting the picture graphically and authoritatively before the President and Mr. Mellon. The memorandum which I have prepared for Mr. Mellon, and the data accompanying it, will, I believe, throw much light on the facts. But this will be incomplete without the views of Messrs. Houghton and Gilbert as to this whole situation.

Would it not be possible to have these gentlemen come home for a short visit to talk matters over? I am satisfied that no more than a word from Mr. Mellon to Mr. Gilbert would bring him home by the first boat. And, of course, the President can summon Mr. Houghton at any time. I do not like to suggest this in any official way, or in a way to give the impression that it has been suggested to me, but I am very sure that the matter is in their minds and that both of them stand ready to come.

Yours very sincerely,

Honorable Garrard B. Winston,
Under Secretary of the Treasury,
Washington, D. C.

Permanent Record Copy

Original handed to Mr Mellon
by B. S. on 9/22/25

Copy handed to Mr Winston in
New York by M. S. B. on 9/22/25

PERSONAL AND CONFIDENTIAL

September 21, 1925.

Dear Mr. Secretary:

While in Europe, a cable from my office advised that Mr. Winston desired a report from me for your use, which I now have pleasure in making. I was also asked by the American Ambassador in London to secure certain information in regard to the war debts, which I conveyed to him verbally. My trip afforded many opportunities to gain an insight into conditions, especially as they bear upon the subject of debt funding, and these impressions, together with the information which I gave Ambassador Houghton, I shall now attempt to express in this letter.

Much of what follows is confidential and knowledge of the existence of this report might, indeed, cause me considerable embarrassment. I am therefore asking that it be treated as a confidential document, for your use, and for the President's if he desires to read it.

I have made it relate particularly to the French position because of the pending negotiations. But it can be elaborated with comments in regard to the operation of the Dawes Plan, which, of course, has a bearing upon debt funding. I will be glad to write a supplementary statement if you desire me to do so.

Attached is a translation of a confidential statement which was furnished to me by the Governor of the Bank of France. This letter is in part based upon that statement.

CONDITIONS IN FRANCE

General Conditions: It is probably true that the people of France are well employed, and reasonable prosperity is returning measured by French prewar standards of living, whereas the Government of France is impoverished, if not struggling against bankruptcy. This is in contrast with the situation in Germany,

where the Government, being relieved of its debt, is fairly prosperous, but industry and commerce are not so profitable, and the people not so prosperous.

On the whole, this year's crops have been good; better than last year, although some losses resulted from heavy rains at harvest time, principally to vegetables, late grains and fruits. There is serious depression in the wine industry of Southern France due to some deterioration in the condition of the vines, but principally to the large expense of harvesting.

Except for the "Nord," all the railroads on which I traveled were in bad condition. The Nord line is largely owned by Edouard de Rothschild, who has probably had sufficient means to finance the maintenance of the road. But there were some twenty wrecks in a period of thirty days, mostly due to bad track conditions and running trains too fast.

Friends who have motored throughout France tell me that the motor roads are also in bad condition, not being kept in the good repair of prewar days.

The national monuments of Paris have been the pride of the French, but there is evidence that they are not being maintained. While Mr. Rockefeller has provided for repairing the Palace of Versailles, the grounds are not maintained and are rather a depressing spectacle of weeds and underbrush. I was also told that the Palace of the Louvre and other important public buildings are in bad repair.

While I had no chance to see more than a small part of the devastated areas, I am told that reconstruction work is about completed as to farm lands, public buildings, railroad stations, canals, many churches, and the more important business and industrial plants. Also as to a large number of the private dwellings, although many dwelling houses still require rebuilding or repairing. Further work of reconstruction has now been almost entirely suspended.

These evidences of national economy indicate the straits of the Government caused by their budget deficits and difficulties with the floating debt.

The people of the nation, however, are certainly at work. I am advised that

there is practically no unemployment of consequence, and labor is even being imported from Italy and elsewhere for the harvests.

The figures of the visible balance of trade continue favorable, but too optimistic conclusions might be drawn from this condition. The progressive depreciation of the franc acts as a strong stimulus to exports, and the nation is liable to experience a sharp temporary reversal of trade conditions whenever the currency is reorganized and stabilized. Another allowance must be made for a factor which is not commonly known. France includes in export figures all exports to her own colonies, including particularly French Indo-China, to which she exports largely. But the monetary systems of the French colonies are, in fact, tied to the monetary system of France, and consequently exports to the colonies do not produce a true balance of payments. Of course exports of the colonies to the rest of the world, which are not included in export figures, would, in part, offset this. But it is nevertheless a fact that payments for exports from France to Indo-China are made in her own currency, therefore serving to swell what appears to be a favorable balance of trade without producing the foreign exchange needed to protect the franc.

There is no doubt that standards of living have been reduced. French people who live in the provinces, in former years were accustomed to spend a season in Paris, attend the opera, do their shopping, and visit friends. They are no longer able to pay the hotel rates, nor the prices charged at the best stores and restaurants, so they no longer go to Paris. But the flood of European travel from North and South America has reached proportions heretofore unknown, and has kept Paris fairly prosperous.

There are some evidences of an upward movement in wages, and especially in salaries and wages among the more helpless classes. A serious strike of bank clerks was in progress while I was in Paris, which had extended somewhat throughout the country. The postal clerks recently struck for pay increases, and got them. If

some such increase becomes general, especially in the Government Service, it will add to the difficulties with the currency. Any general wage increase will likely be followed by some price increases in the provinces where they have not yet risen to city levels, still further adding to the difficulties of the currency problem.

A curious situation has resulted from the immense deliveries of reparation coal by Germany. Coming as this does with greatly enlarged use of oil and hydro-electric power, there has been an unwieldy accumulation of surplus coal; and the coal business of Europe is withering. Hydro-electric development is active all over France, Germany, Switzerland and Italy. Switzerland, for instance, includes in her export figures "Receipts from Power Transmitted Over the Border," which is now considerable. Railroad lines are being electrified in many districts where water power is accessible. A large percentage of the Suisse railways are now being electrically operated, and it looks as though in time a large part of the main lines of the French railways will be operated by electricity. This presents a gloomy outlook for the coal business and the extent to which reparation payments in that form can indefinitely continue. I have been told by members of the reparation organization that in order to convert coal deliveries into cash, the French are disposing of reparation coal at 30%, or even more, below the price at which Germany gets credit. And, in fact, it is not impossible that the entire credit on reparations for deliveries in kind to the French would need to be discounted from 20% to 30% in order to ascertain what the French are actually realizing.

Taxation: A fairly elaborate explanation of the French system of taxation appears in the document attached, which will not, however, be wholly intelligible without better understanding of the difficulties of taxation which arise largely from the psychology of the French people. Too many critics of French finance abuse the French Government for its failure to collect taxes without any understanding at all of the French people. Limitations upon what a Government can collect in taxes are partly what the people are able to pay, but equally what the people are willing to

pay. The French nation has always relied upon indirect taxation, as have the other Latin countries, whereas for many years the Anglo Saxons have been educated to regard direct taxation, proportioned according to capacity, as the more just system. The French had no direct income tax before the war. Therefore, in estimating what is possible in the way of taxation in France, we should face the fact that we are dealing with Frenchmen, and not with Anglo Saxons, and recognize that limits of taxation are somewhat fixed by the ability to pay taxes, but quite as much or more by ability to collect them. The psychological limitations of taxation in France are low compared to what they are in Anglo Saxon countries. The peasant classes are largely small agriculturists; that is to say, property owners and savers. They are conservative, thrifty, and secretive. And it is impossible to get them to make a tax return. They will pay taxes on their land, but not on the concealed results of their thrift. The farm peasant is a quiet fellow, who stays at home, works hard, saves his money, and largely escapes taxation. The other class which probably escapes a fair share of the burden of taxation is the wealthy businessman, who has the means of concealing his income. Undoubtedly, a great variety of expedients are employed, even, I am told, to the extent of keeping a separate set of records upon which to base a tax return. But escape from taxation by this class is even more serious than that of the peasants, as it is the wealthy businessman who is able to send his earnings out of the country and keep them invested abroad, without taking the income home. It not only deprives France of tax revenues, but reduces the working capital of the nation at a time when it is badly needed. This is a situation which cannot be corrected over night, but, in my opinion, will be corrected if the debt funding operations are completed; if they make due allowance, as they should, for the peculiarities of the French temperament, and afford the French Government opportunity for increasing direct taxation gradually, rather than suddenly, and so avoid a flight of capital out of the country, or a more extensive hoarding of the currency.

On the other hand are the classes having socialistic tendencies, - the wage earners, the salaried classes, the professors, lawyers and the like, - many of whom are active and aggressive socialists. These are constantly pressing for capital levies. And that is the one way to frighten the French peasant, and get him to conceal his savings.

There are evidences, however, that taxes are being more vigorously collected, and that the program of enlarging the area of taxation is being more vigorously developed. Monsieur Simon told me that in a large bank like his own, the "Societe Generale", they have good opportunity to observe much improvement in the thoroughness with which tax collections are now being made. It is one of the largest banks in France, and covers most of the industrial section with a network of branches.

All of my talks with Frenchmen indicated that outside of the agricultural classes they are now feeling the burden of taxation more heavily. My friend Baron de Neuflyze, a banker and one of the regents of the Bank of France, told me that he paid 60% of his income in taxes to the Government. They are also embarrassed by inability to deduct business losses (that is capital losses) from current income as we do, and consequently many firms and businesses are obliged to amortize losses over a period of years. As illustrating the burden of the inheritance tax, the Governor of the Bank of France told me that he had recently been left a legacy of 1,000,000 francs by a second cousin, and after calculating the amount of the tax, the expense of administration, etc., he found that there would be nothing left and he relinquished the legacy entirely to the State.

But in considering the capacity of the French people to pay taxes, it must also be borne in mind that standards there are much lower than with us, or even in some other parts of Europe. To illustrate, Monsieur Parmentier employs a man and his wife to run his apartment, who do all the work, the man also taking care of an automobile. Even though he has increased their wages two or three times recently to meet the in-

creased cost of living, he is today paying them only 525 francs a month, or, say, \$25. gold. While I was in Paris Colonel Logan rented a new house with an obligation to employ the owner's chef and butler. The chef receives the gold equivalent of \$12. a month, and the butler \$10. These are wages paid in the city of Paris. They are lower in the provinces. A recent report on salaries of bank clerks shows that they receive an average of 800 or 900 francs a month (\$40 to \$45 gold) even in the higher grades, on which they must support a family. But even these wages are better than those paid in Italy, where an American family I know of, now living in Rome, employs twelve servants whose aggregate salaries are not equal to what I pay my valet.

If the economic rule prevails in France that wages and salaries equalize themselves to relative levels between the different classes, these indications of the low standard of reward of labor in France are likewise some indication as to the burden of indirect taxation, which adds to the cost of living of all classes, as well as of the meagre capacity of the nation as a whole to pay heavy taxes.

Too little consideration is given by critics of the French of general impairment of capacity to pay taxes because of war losses. These are not confined to the destruction of industrial establishments in Northern France and to long idleness in production while restoration work was taking place, but to direct losses of the French people in foreign investments. It is estimated that no less than \$4,000,000,000 was lost by French investors in Russian securities which have been wiped out, and total losses on foreign investments, the value of which was destroyed or impaired by the war, is placed by some estimators as high as \$6,000,000,000.

On the other hand, even with the increased taxes and reduced expenses, the budget has not yet been balanced, and that, together with the embarrassment caused by the large maturities of floating debt has led to many current reports that the Government is not paying its bills promptly.

There is a strong argument, not commonly considered, however, in support of

the belief that the French people can pay heavier taxes than they are now paying. The annexed statement shows that the combined budget and supplementary budget in 1914 aggregated 6,260,000,000 francs gold, and that the budget of 1925, reduced to a gold basis by using a ratio of four francs to one, totals 9,770,000,000 francs, which, on a gold basis, is an increase of only about 50% over prewar.

In England the prewar budget ran at about \$900,000,000 gold, and the present budget runs roughly at about \$4,000,000,000 gold, or four to five times the prewar budget.

In other words, if the purchasing power of the French currency has been reduced to one-quarter of its prewar value, the burden of the debt must be but one-quarter as heavy, provided, of course, the purchasing power of the franc is correctly represented by the ratio of four to one. Unfortunately in a nation like France, where a large part of the industry is conducted by craftsmen, rather than by large organized units, wages do not advance as rapidly as the value of the currency depreciates notwithstanding that the cost of living does advance quite rapidly. The present index number of prices in France is over 500. This results in impoverishing large classes of people, who, nevertheless, must meet an unduly heavy proportion of the tax burden because indirect taxation is so largely employed rather than direct taxation.

The solution of the whole tax problem for France is, probably, to gradually increase the taxes of the agricultural classes, and collect much heavier income taxes from the wealthy classes. But it must be done gradually! This latter class, just as the former, has many means of escaping taxation. They send their money out of the country, whereas the peasant hoards and conceals his savings in bank notes.

The Public Debt: The attached statement gives an analysis of the position of the public debt. Reference here need only be made to the statement on page 5, which indicates the volume and rate of turnover of short obligations issued for one, three, six and twelve months, and on page 6 et seq., showing the weight of maturities

at the end of this year. On the 25th of September 3,250,000,000 francs mature, and on the 8th of December 10,000,000,000 francs. These maturities, together with the recent embarrassment of the Bank of France, led to the radical measure of issuing the stabilization loan in the form of a perpetual rente bearing 4% interest, to be paid in paper francs but at such a rate that the holder will always realize not less than 95 francs per pound sterling.

Ceillaux's present effort to deal with the floating debt was the result of a choice of four possible measures:

- a. A capital levy
- b. An enforced conversion
- c. A further inflation of the bank note issues
- d. An obligation issued on a gold basis.

Plan (a) would likely have caused a flight of the franc, as it did in Switzerland when a capital levy was threatened. Plan (b) would have had a somewhat similar effect and have been a severe blow to French credit. Plan (c) would have started progressive inflation. And plan (d) was the choice of evils.

The expedient is a dangerous one, for if the franc suffers a further decline it means that progressive inflation of the currency will be necessary after meeting this obligation, in order to meet the subsequently maturing obligations which naturally cannot be refunded on any less favorable basis. There are many responsible Frenchmen familiar with finance who today have abandoned their belief that the nation can support its public debt with the franc worth as much as 100 francs to the pound. They think it may have to go to 120, or 150, or even to 200 francs to the pound. It is now about 103 to the pound. This is counsel of despair, but it is not out of the question that something of that sort will develop if the pending loan is a failure and supportable debt settlements cannot be effected with the United States and England.

Many rumors regarding the success or failure of the loan were heard while I was in France. Some statements placed subscriptions as high as 20,000,000,000 francs;

Others stated that it was a complete failure except in the city of Paris. The amount really required is about 40,000,000,000 francs; and the Government hoped to get a minimum of 20,000,000,000 francs. The last statement which I received, while in London, which is probably too low, indicated that total subscriptions were then between 10,000,000,000 and 11,000,000,000 francs.

The Bank of France can still increase loans to the State by over 3,000,000,000 francs, and their note issue by over 5,000,000,000 francs. This may enable them to meet the September situation, but will result in further inflation, further depreciation of the franc, and might induce a further export of capital at a dangerous rate.

The Bank of France: The position of the Bank illustrates the difference between our scheme of war finance and that practised by the European nations in varying degree. With the exception of a loan of \$50,000,000 made by the Reserve Banks to our Treasury immediately after war was declared, our Government has borrowed nothing directly from the Reserve Banks, except advances to finance the turnover on quarter days, which are always paid off within a week. Consequently, all of the war loans of the Reserve Banks were upon the private obligations of individuals and institutions. The Reserve Banks were left in control of the money market through their discount rates, and the banking system was able to absorb the enormous importations of gold without dangerous inflation. The gold simply paid off the borrowings of our members. If the Government had borrowed, it might not have been willing or able to repay as rapidly as our bankers did and the imported gold would have caused an immense inflation.

In France, as with other Allied Governments, too large a proportion of the Government borrowing was from the Bank of issue. The Government cannot repay the Bank, and the Bank is left helpless to control the domestic monetary situation. Great Britain escaped the worst of this development, but still has to deal with the currency notes. Germany cleared the decks by abandoning the old currency and re-

organizing the Reichsbank. The Banks of Issue of France and Italy are helpless, however, because their portfolios are almost entirely loans to the State. The Bank of France, in round figures, has loaned the State 30,000,000,000 francs. Its private portfolio consists roughly of 3,000,000,000 francs "Lombard loans", secured by investment bonds, - say, \$150,000,000. These loans are made at the head office and branches all over France, and are not of sufficient volume to exert any influence upon monetary conditions if the bank rate were raised. The portfolio of "bills discounted" - about 3,000,000,000 francs - is almost entirely composed of short bills deposited for collection and payable within five or seven days. On one of the days I was at the Bank, the discounts presented were 256,000,000 francs, of which only 8,000,000 were long bills, all the balance being simply collection items. This leaves the Bank literally helpless; its main function is merely to cut up Government bonds into small denomination notes to circulate as money.

The government of the Bank is also of a character to add to the difficulties. While the regents are elected by the stockholders, the Governor and Deputy Governor are appointed by the State. The directors can do nothing without the assent of the Governor, and the Governor can do nothing without the assent of the directors. It results in the influence of the State being superior to the influence of the directors. When the records of the Bank were recently falsified under a previous cabinet, I am told that it was due to an urgent appeal that if the regents resigned, as one or more of them threatened to do, the nation would be wrecked financially because of the resulting alarm. Under the conditions described, criticism of the recent reduction in the discount rate from 7% to 6% loses much of its force.

Politics: My understanding of the present situation of the Painleve Government, gathered from many sources, is probably reasonably accurate. The "majority" includes many socialist votes, - those of the "left." The Government is dealing with many difficult questions; these are the Riff war, the rebellion in Syria, the domestic debt situation, the foreign debt funding, and the negotiation of the

security pact. The socialists do not wish to shoulder the responsibility of dealing with these questions and are quite willing to allow the present government to do so, the radicals simply retaining the right of approval or disapproval. There seems to be general expectation that after Parliament reassembles in October, say by the middle of November, this government is likely to fall, and a more radical government take its place. Briand is supposed to be manoeuvring to secure the radical vote and form a government himself. Caillaux on the other hand, is making a superhuman effort to deal with the financial difficulties in the hope that he may experience success and be asked to form a government himself. The probability seems to be that this may happen after a short interval of a more radical government, under some man like Briand, with Violet as Finance Minister.

THE FRANCO-BRITISH DEBT NEGOTIATIONS

The following I believe to be accurate. It is based upon my memory of many talks with responsible people during which it was impossible to take notes.

Caillaux's first position was to insist that payments be wholly conditioned upon the product of the Dawes Plan; that any development such as a decline of the franc which indicated that France was paying beyond capacity would be dealt with by some plan analogous to the Dawes Plan. His offer was an annuity of 10,000,000 sterling for sixty-two years.

The British position was to require an unconditional annuity of 16,000,000 sterling. This was partly the result of a study of estimates and figures submitted by experts, but was finally arrived at by a rough calculation which attempted to reconcile the probable results of the Dawes Plan, the principles of the Balfour Note, and the commitments made by Winston Churchill in his speech in Parliament last December. The Dawes Plan was roughly estimated as capable of producing one-half of the normal annual payments of 125,000,000 sterling, say \$300,000,000 per annum. The French share of these payments, say 52%, would theoretically be about \$150,000,000

although actually it would be much less than this on account of the priorities, and on account of the discount on deliveries in kind mentioned elsewhere. Upon this estimate the compromise figure of 12,500,000 sterling was finally arrived at for the British annuity. A like proportion on the American debt would be about 16,000,000 sterling, - the two together approaching the estimated receipts by France from Germany.

The Balfour Note laid down the principle that Great Britain should collect as much on debts owing to her as she was required to pay under the American debt settlement. The British figured that 12,500,000 sterling, plus payments which they would receive on other debts, plus their share of the annuities under the Dawes Plan (probably figured as producing more than the estimated 50%) would roughly approximate the amount required to meet the American payments.

As to the promise made in Parliament by Churchill in December, that payments to Great Britain should be *pari passu* with other creditors, the view was expressed that a debtor threatened with insolvency could not prefer one creditor over another, but that the creditors might themselves agree to accept respectively more or less one than the other, if that was agreeable to the debtor. But the tentative agreement did not commit the British to accept less proportionately than what the United States is to be paid.

Caillaux strongly emphasized the transfer difficulties, and insisted that that was the controlling factor. He proposed that if transfer difficulties arose reference should be made to a committee consisting of the Governor of the Bank of England, the Governor of the Bank of France, and the President of the League of Nations. Objection was made that such a reference would only disclose the facts of the situation at a given moment, but would not correct causes leading to that state of facts, such, for instance, as might arise from abuse of the Bank of France, evidence of the possibility of which had already been specifically given to the world. The question could not be settled and was left open for future negotiation.

Caillaux also insisted that there must be a moratorium, or very easy payments at the outset. While the rate of payment was not settled, it was agreed that payment would be graduated, starting possibly at 2,000,000 sterling, and increasing slowly until the full annuity was reached after the Bank of England loan (referred to later) had been fully repaid. The schedule of payments is to be arranged later.

Caillaux further insisted that payments be dependent upon the amount collected from Germany.

In principle the British are willing to make some concession on this point. Mr. Churchill intimated to me that probably a fixed annuity of 10,000,000 sterling, with 2,500,000 conditioned upon German payments would be acceptable. But I surmise they might make a smaller fixed payment and a larger contingent payment if pressed by the French, rather than see a failure of the settlement.

The lump sum figure arrived at as a compromise was undoubtedly the result of the intervention of Downing Street. The Chancellor's point of view was frankly that of the Treasury, and of the British budget. Mr. Chamberlain's point of view was more largely political. He is at present negotiating the security pact, to which they attach the greatest importance. The influence of Downing Street was to moderate the payments as some aid in facilitating successful negotiation of the pact. The details of the discussion I am not acquainted with, but it was that influence which led Mr. Churchill to agree to reduce the annuity.

I think the situation may be fairly expressed by stating that while a smaller payment to the United States proportionately than the proposed British annuity would be gratifying and helpful to Downing Street, it would not be so pleasing to Whitehall. But nevertheless, I have the feeling that while Whitehall would try to insist upon increasing the British payments *pari passu* with American payments if the latter are larger, Whitehall might be persuaded to make even a further reduction in the British payments if the American payments were proportionately smaller. This might take the form of a reduction in the portion of the annuity which is fixed, and an increase in

the portion which is contingent upon German payments.

In addition to the payments to the Bank of England, and the proposed annuity to the British Government, there is at present being paid (and I gather will be continued) about 1,000,000 sterling for supplies sold France, similar to the payments now being made to the United States.

I understand that the actual amount of cash advanced to France by the British Government, without any interest included, was 470,000,000 sterling in round figures. Interest has been added to capital at the Bank of England discount rate, whatever that might be from time to time, thus increasing the principal to the present amount of about 630,000,000 sterling. The amount of this debt is further again affected by gold transactions. Before the United States entered the war, an arrangement was made between the British, French, Russian, and (subsequently) the Italian governments by which each contributed an amount of gold to be shipped to America in payment for war supplies. According to the published statements of the Bank of France, the amount which it furnished should be estimated at about 70,000,000 sterling. This, as I recall, is the balance of the amounts of gold shown as "held abroad," less the amount to be repaid by the Bank of England. But Mr. Churchill told me that the amount was 50,000,000 sterling. Probably no difficulty would be had in getting exact figures. This gold, whatever may be the amount, has been treated by the British Government as "borrowed" gold, although the entire amount, together with the Russian and Italian gold (and some I believe from Egypt) was shipped to the United States in accordance with the arrangement originally made. The British Government has been allowing interest to France upon the amount of this gold and the interest has been credited on the interest charged against France on the entire amount of the loan. It is in the nature of a bookkeeping entry.

The new arrangement contemplates that a non-interestbearing note will be given representing the entire amount of the gold, which will be repayable at the end of sixty-two years, and when repaid, the French are to get back the gold. This

is eye-wash to save the statement of the Bank of France. I very much doubt if it ever is actually paid. Caillaux probably feels that the arrangement is temporary to protect the Bank of France against any panic among the peasants who hoard Bank of France notes, which might result from so considerable a reduction in the nominal gold reserves of the Bank as would be necessary if this gold were credited on the French debt to Great Britain, and the technical right of the Bank of France to its return be thereby terminated.

The British would have preferred to join the United States in a settlement with the French. They did not consider that any settlement with an insolvent debtor, or one of doubtful solvency, would be tolerated which did not result in payments *pari passu*. As such a joint negotiation was not possible, however, they did the best they could and strongly hope that the American settlement will at least be along similar lines, but with necessary adjustments of details and less important matters, so long as the basic principle of this settlement is observed. They estimate that their settlement will effect repayment of the principal and not over 2% interest.

Mr. Churchill explained to me at great length his difficulty in dealing with the British debt so long as the American debt settlement was incomplete. He seemed to have been considerably disturbed by the adverse comment from America, and the inference that in some way the result of the negotiations created a trap for the United States, or operated in some way to circumscribe the freedom of the United States in dealing with France; or some such thing. He asked me if I would state to you in his behalf, and from him, that there was not the slightest intention of causing any embarrassment, or of placing any limitation upon the freedom of action of the American Government, and that rumors to that effect should be disregarded.

The British think the French capable of making these payments if Germany makes substantial payments under the Dawes Plan, but admit that there is some uncertainty even then. The question of capacity to effect transfers must be examined and dealt with later, and will undoubtedly present great difficulties. There would be little

dissent, however, that if the British settlement is not followed by a somewhat similar settlement in America, and, following that, a monetary reorganization, there is still danger of a breakdown of the franc which would make the present settlement ineffective, and put the whole matter back in its original position. The perilous situation of the French floating debt is not minimized, but hope is still expressed that this can be dealt with satisfactorily if the external debts are funded, and if confidence is improved by the successful negotiation of the security pact. On the other hand, the conversion loan is regarded as imposing on the Treasury the necessity for hereafter conducting all of its refunding on some such stabilization basis. The pending scheme of 95 francs to the pound may mean a later loan with a higher rate per pound, - and so on with a possible increasing depreciation of the franc. The only solution is a monetary reorganization, recognizing the need for revaluation, and regularizing it by law.

If the pending maturities of French domestic loans are not met by some refunding loan, the only recourse of the Government will be to the Bank of France. Each resort to fresh issues of paper money will mean depreciation of the franc in terms of sterling and dollars. The service of the annuities to the United States and Great Britain will again cause further emissions of paper money by the Bank of France, and the resulting progressive depreciation of the foreign value of the franc must inevitably lead to a suspension of foreign payments.

BANK OF ENGLAND LOAN TO BANK OF FRANCE

References are frequently made to the so-called "commercial" debts of France.

They appear in the attached memorandum in three categories:

1. The commercial loan extended to the Bank of France by the Bank of England.
2. The obligation of the French Government to the American Government for war and other supplies sold to France after the armistice.
3. All other debts of this general character.

[As to the debt of the Bank of France to the Bank of England: I first became acquainted with the existence of the loan, as I recall, in 1919, and at that time was told that it was made, doubtless after some negotiations between the Governments, for the purpose of financing trade between the two countries. France was in great need of supplies for her people; credits had been withdrawn in London; the French had no means of paying; and this loan was expected to meet the emergency. I am not aware of what was done by the British Government to indemnify the Bank of England.]

The loan was originally 72,000,000 sterling, and as part of the collateral the Bank of France delivered to the Bank of England 24,000,000 sterling in gold, which was to be returned as the loan was repaid *pari passu* with repayments. France has been making regular payments in the past of both principal and interest and receiving equivalent amounts of the gold in return, 6,000,000 sterling gold having been so delivered. Roughly 18,000,000 sterling is still to be returned, and the principal of the loan has been reduced to about 48,000,000 sterling. The gold is held as collateral and does not appear in the statement of the Bank of England.]

A new arrangement for repayment has now been tentatively effected, by which the balance of 18,000,000 sterling in gold will be held until the loan is entirely repaid, when it will be returned to the Bank of France. The entire amount of principal at the proposed rate of repayment will be liquidated in 1930. The schedule of payments given in the attached memorandum, I gather, are those under the old plan of repayment, which will now be modified, payments starting somewhere in the neighborhood of 4,000,000 sterling and increasing until the year 1930. I have not the exact figures.

Whatever may have originally been the relations between the two governments in connection with this loan, its present bearing upon the debt adjustment lies in the willingness of the British Government to forego larger payments from France during the first five years while the debt to the Bank of England is being repaid, so as to

void too heavy a burden of transfers, and this, of course, gives the Bank of England what is in the nature of a preference over the Government.

My understanding has been that the interest on the Bank of England loan has been the regular bank discount rate from the beginning, whatever that may be.

This matter was, I believe, explained verbally to both Mr. Gilbert and Mr. Wadsworth when they were connected with our Treasury.

THE GENERAL PROBLEM OF INTERNATIONAL PAYMENTS

The payments now being made by foreign governments to our government, including Belgium but excluding France, somewhat exceed \$200,000,000 per annum. We estimate at the bank that the service of foreign loans taken by American investors since the conclusion of the war will call for further payments of about \$200,000,000 and many of these, of course, relate to loans which are wholly unproductive for the borrowers.

Payments to be made by Germany to her creditors next year will, theoretically, amount to around \$300,000,000, and Germany will not have the proceeds of the Dawes Loan to draw upon for the purpose.

In a general way it may be stated that the facility with which these international transfers were made last year was mainly due to the extent to which credit was extended by the investors of the United States. In less than two years they have taken \$2,000,000,000 of securities of foreign origin. This enabled foreign purchasers of American goods, especially of the increased exports of cereals last year at high prices, to make payments in America, and it undoubtedly was the principal means for enabling Germany to meet her payments, and, in turn, the British, French, and others to make payments to us. It was a development which I regard as essential to European recovery, and greatly facilitated monetary reconstruction and stabilization in exchanges, so essential to the continuance of our foreign trade.

But it must not be overlooked that if any change in conditions in the investment or money markets, or if any shock to the confidence of American investors

in foreign securities, especially European, should arise, such as might indeed be the case if a French default should occur, or if the negotiation of the security pact were a failure, then the closing down of the American investment market to the rest of the world would considerably imperil the continuance of these foreign payments.

The great importance of the American investor, and his absorption of European securities, in enabling these debt settlements to proceed in an orderly fashion is not sufficiently emphasized in discussions of this subject.

CONCLUSIONS

There are certain unescapable conclusions to be drawn from what I have observed abroad, which I will briefly summarize:

1. That the domestic debt of France, so large a portion of which is of early maturity, is a menace to the Government's credit, and, consequently, a menace to the Bank of France. It contains the possibility of a complete breakdown of their monetary system, necessitating much more radical measures than those which are now under discussion or being attempted.
2. That the limitation upon the ability of France to make foreign payments is less a problem of transfers; (that is finding the amount of foreign exchange necessary to meet obligations) than it is of collecting sufficient taxes in France to enable the Government to acquire the foreign exchange without inflating the currency.
3. That what the State needs is a thorough-going financial reorganization and funding of the short debt, which should be accomplished by domestic loans and not by foreign loans.
4. That the expectation that France might rely upon anything like the maximum of \$300,000,000 a year from Germany will prove illusory for some time, if not entirely so, as can readily be shown by a study of the recent report of the Reparation Agent, and by consideration of the various difficulties with which Germany is now struggling, which are not, however, touched upon above.

5. That the present plan of funding the debt to Great Britain with an annuity of 12,500,000 sterling, if followed by a refunding of the American debt upon approximately equal terms, would impose a burden of payments upon France which she is not at the present time likely to be able to meet in full, unless recoveries from Germany are greater than expectation justifies, and payments are graduated for some years.

6. That an obligation to pay annually at once to the United States and Great Britain any large sum such as \$125,000,000 to \$150,000,000 will too likely be followed by an inflation of the currency, and resulting inability to make transfers.

7. That the closing of the British investment market to all foreign loans except her own colonies and the nations being reorganized under the finance section of the League of Nations, has closed the only market, outside of the United States, where France could borrow; and that in consequence, the attitude of our government in restraining our bankers from negotiating French loans in the American market, and at the same time insisting upon debt funding, has placed the French Treasury in a vise, from which there is no escape except by repudiation, or by meeting any terms we may exact.

8. That we must accept the fact that we are dealing with the French people and not with Anglo Saxons, and meet the peculiarities of the people of that nation, which would indicate the necessity for small and gradually increasing payments at the outset, until the maximum is reached, say, thirty-five or forty years hence, or even later, after which time the rate of transfers should gradually be decreased in order to avoid the serious readjustments which would be necessary were transfers to be entirely discontinued at the period of maximum payments.

9. That if some such plan is adopted, the burden of taxation in France is not so heavy but what repayment of principal and some interest could be effected. Gradual increases in taxation (the only plan likely of success) would actually be facilitated by the need for meeting gradually increasing payments.

10. That a successful negotiation along these lines would also facilitate the management of the domestic debt, and might even be followed by a reorganization of the currency to a stable basis, so that prices, true wages, the burden of debt, and the cost of foreign currencies will not be constantly fluctuating.

// As you have doubtless been advised, the National Bank of Belgium and the Belgian Government have a fairly well matured plan for dealing with their own monetary problem, which I had an opportunity to examine with the Governor of the Bank in some detail. The funding of the Belgian debt to the United States now presents the opportunity for them to carry out their plan, which I have little doubt will be successful, and an example to France. If this could be followed by a similar reorganization in France, especially if political tranquillity is insured by the negotiation of the security pact, I believe we can look forward hopefully to the approach of the last stages of economic recovery in Europe.

I hope that the foregoing may prove to be of some value in dealing with this difficult matter.

Faithfully yours,

Honorable Andrew W. Mellon,
Secretary of the Treasury,
Washington, D. C.

Encs.
BS.NSE

The "open credits" of the French budget were,

In 1914	5,191,600,000 francs
In 1925	8,280,000,000 francs in gold

(basis 20 francs to the dollar).

The "anticipated receipts" were:

1914	5,191,900,000 francs
1925	8,290,000,000 gold francs

The "budgetary expenses" which represent, in 1925, an increase of 67% in comparison with 1914, show, nevertheless, diminutions in most of the categories, notably: 537,200,000 gold francs for the Army and Navy and: 335,100,000 francs for the expenses of Government and collection. The increase in the expenses is caused almost exclusively by the charges for the public debt, which increases from 1,306,600,000 francs to 4,640,000,000 gold francs, to which must be added 384,000,000 gold francs for advances to the pension fund, making a total of 5 milliards of gold francs nearly.

The comparison of these budgets shows, moreover, that the direct taxes have been much more increased than the indirect taxes, taxes for consumption and fiscal monopolies. The direct taxes provided one-half of the normal resources of the general budget, just as the tax on incomes represents more than half of these direct taxes.

Moreover, exceptional receipts: the contribution on war profits, the liquidation of stocks which figure in the budget of 1925 for more than 300 million gold francs are bound to disappear.

From 1926 on it must be anticipated that the budget will have to be raised to 35 milliards and a half, nearly, to be balanced, that is to say that it will be necessary to increase taxes from 3 milliards to 3 milliards and a half of francs. It must be added that the management of the external commercial debt, which was

reckoned in the budget of 1925 at 1,100,000,000 francs, will call, in reality, for the actual paying out by the Treasury of more than 2 milliards and a half of francs, as the amounts for paying off were only provided for for one portion of the debts and the rates of conversion were established at exchange rates which must be increased today by more than 20%.

**INTERNAL AND
EXTERNAL DEBT**

The internal debt of France is made up as follows:

	<u>1918</u> Frs.	<u>1924</u> Frs.
Perpetual and long term debt)	67,779,000,000	148,194,000,000
Short term debt)		39,844,000,000
Floating debt	<u>56,015,000,000</u>	<u>90,488,000,000</u>
Total	123,794,000,000	278,526,000,000

To these 278,526,000,000 there must be added 715,000,000 six-year loans which must be paid to the injured between August 16, 1925, and February 16, 1928.

The external debt (on November 30, 1924) amounts to:

a) Political debt:	
United States	15,194,000,000 gold francs
England	<u>15,816,000,000</u> gold francs
Total	31,010,000,000 gold francs
b) Commercial debt	<u>5,017,000,000</u> gold francs
Total external debt	36,027,000,000 gold francs
	Or 144,108 million francs.

Total of the external and internal debt:

423 to 423 milliards and a half of francs.

REPARATIONS

The net receipts, on account of reparations and damages which the French Treasury has received since the Armistice, up to July 31, 1925, amounted to about million 530/gold marks, or 2,650,000,000 francs, while at the close of 1924 the amount of damages paid by the French Treasury amounted to 129 milliards of francs.

The Direct Taxes, whose importance has been shown above, comprise:

1) The succession tax amounting up to:

For 3 children alive or represented:	9%
For 2 " " " "	14,40%
For 1 child " " "	25,20%
No children	46,80%

2) The transfer duties (likewise a matter of inheritance) amounting to:

From parents to children	20,40%
From uncle to nephew	58,80%
From relatives beyond the fourth degree and from persons that are not related	70,80%

3) The taxes on incomes (cédulaires), which call for certain deductions at the beginning (for example, 350 dollars, salaries and wages, 150 dollars for married tax payers if their wives have no personal revenue, and 150 dollars per child of less than eighteen years if it does not receive wages) are as follows:

	<u>Rate for</u> 1925 %	<u>Rate Proposed</u> for 1926 %
Income from personal property:		
French corporations	12	20
Foreign corporations	18	25
Land taxes	12	
Industrial and commercial profits	9.60	15
Agricultural profits	7.20	10
Professional profits, non commercial	7.20	10
Salaries and wages	7.20	10

4) The general tax on incomes rises as high as 44% and is increased, when the tax payer is above 30 years of age, for bachelors or for tax payers who have been married two years and are without children.

Indirect taxes. They are extremely numerous and affect all forms of production, consumption and the circulation of wealth.

AMOUNT OF TAXES PER
CAPITA OF INHABITANTS

If the taxes paid in France per capita of inhabitants are reckoned at \$39.07 and the national revenue of France, according to rather exaggerated estimates, at 127 milliards of francs, or \$6,350,000,000 (\$161 per inhabitant), the taxes paid by the French represent 24.20% of the revenue as compared to 23.2% for England and 11.5% for the United States, according to the valuation of the New York Trust Company.

COMPARISON OF THE BUDGETS OF 1914 AND 1925

<u>Credits opened</u>	Budget of 1914	Budget of 1925	
	(In millions)	In paper francs (and hundreds of thousands)	In gold francs (Rate 4 to 1)
Public debt	1,306.6	18,573.6 ⁽¹⁾	4,640 ⁽¹⁾
Public offices	20.0	44.5	10
Public services:			
Army and Navy	4,717.2	4,718.9	1,180
Other ministries	1,423.5	8,151.5	2,040
Expenses of administration and collection	675.1	1,349.1	340
Sundry expenses	49.3	299.5	70
	<u>5,191.6</u>	<u>33,137.2</u>	<u>8,280</u>
<u>Receipts anticipated</u>			
Taxes on revenue and capital	1,899.5	14,363.6	3,590
Indirect taxes and fiscal monopolies	2,221.1	13,632.5	3,410
State and domain cultivation	484.7 ⁽²⁾	399.1 ⁽³⁾	100
Various products	68.4	451.0	110
Receipts in course	105.0	1,588.2	400
Products obtained in Algeria	2.7	11.5	3
Exceptional resources	(410.5)	(2,705.0) ⁽⁴⁾	(675)
Anticipation of the provisional account	112.5	380.0	95
Emission of Treasury bonds	298.0	"	"
Contribution for war benefits	"	775.0	195
Liquidation of stocks	"	450.0	110
Payments by Germany	"	1,100.0	275
	<u>5,191.9</u>	<u>33,150.8</u>	<u>8,280</u>

ANNEXED BUDGETS, CREDITS AND RECEIPTS

Post Office, telegraph and telephone	"	2,039.4	510
State railroads	859.1	2,160.7	540
Railroads of Alsace-Lorraine	"	984.2	240
Various services	202.2	796.1	200
	<u>1,061.3</u>	<u>5,980.3</u>	<u>1,490</u>

Of which:

Exceptional receipts (emission of bonds or advances by the Treasury)	(424.7)	(760.6)	(190)
--	---------	---------	-------

- (1) If the advance to the pension fund anticipated for 1,537 millions were reckoned the service of the debt would absorb more than 20 milliards of paper francs, or 5 milliards of gold francs.
- (2) Including the receipts for post office, telegraph and telephone.
- (3) Not including the receipts for post office, telegraphs and telephones henceforth put under the annexed budgets.
- (4) Not including the emission of 1,537 million Treasury bonds for advances to the war pension fund.

(Financial Laws of July 15, 1914, and July 13, 1925)

INTERNAL DEBT1. Floating Debt

Bonds of the National Defense

(In millions of francs)

<u>Operations Previous to</u>	<u>Emissions</u>	<u>Repayments</u>	<u>Emissions</u>	<u>Excess of Repayments</u>	<u>Circulation</u>
Dec. 31, 1923	611,323	566,000			54,723
Jan. 31, 1924	7,586	7,420	+ 166		54,889
Feb. 28	6,773	6,980		+ 207	54,682
Mar. 31	7,662	7,822		+ 160	54,522
Apr. 30	7,855	6,183	+ 1,672		56,194
May 31	7,567	6,981	+ 586		56,780
June 30	7,783	8,220		+ 437	56,343
July 31	7,722	7,777		+ 55	56,288
Aug. 31	7,446	7,136	+ 310		56,598
Sept. 30	7,518	6,956	+ 562		57,160
Oct. 31	6,684	6,683	+ 1		57,161
Nov. 30	5,612	5,746		+ 134	57,047
Dec. 31	<u>5,941</u>	<u>8,450</u>		+ <u>2,509</u>	<u>54,538</u>
	697,472	652,934	3,317	3,502	

(Statements taken from the report of M. Louis Dausset (Senate) on the budget of the Ministry of Finance for the fiscal year 1925)

ORDINARY TREASURY BONDS

Circulation on November 30, 1924: 2,855,000,000
of the

At the end of 1924 the partition/bonds of the National Defense and ordinary

Treasury bonds was as follows:

One year bonds:	71%	of the total circulation
Six months bonds:	19%	" " "
Three Months Bonds:	5%	" " "
One month Bonds:	5%	" " "

(Information derived from the inventory of the Situation of France, 1924)

2. Short Term Debt

<u>Date of Repayment</u>	<u>Nature of the Loan</u>	<u>Amount</u> Fr.
Feb. 16, 1925	Bonds of the National Defense, 1915-25	333,671,000
July 1, 1925	Credit National, 1922, 2nd emission	3,290,000,000
Sept. 25, 1925	Three and five-year bonds	8,236,934,000
Dec. 8, 1925	3, 6 and 10 year bonds, 1923, 1st series	10,090,088,000
May 20, 1926	3, 6 and 10 year bonds, Sept., 1923	6,189,455,000
Feb. 1, 1927	Credit National Bonds, 1922, 1st emission	3,019,769,000
Sept. 25, 1927	3 and 5 year bonds, 1922, repayable at 101.50%	Note (1)
July 1, 1928	Credit National, 1922, 2d emission, repayable at 101%	Note (1)
Dec. 8, 1928	3, 6 and 10 year bonds, 1923 (1st series, repayable at 103%	Note (1)
May 16, 1929	Decennial loans, 1919 to 1929	6,183,000,000
May 20, 1929	3, 6 and 10 year bonds (Sept., 1923), repayable at 103%	Note (1)
Nov., 1930	5% 1924 bonds at 10 years	15,000,000
Nov. 1, 1931	Credit National 6%, 1921	500,000,000
Nov., 1931	1924, 5% bonds at 10 years	22,500,000
Feb. 1, 1932	Bonds of the Credit National, 1922, 1st emission, repayable at 105%	Note (1)
July 1, 1932	Decennial loans, 1922-1932	234,000,000
Nov. 1, 1932	Credit National 6%, 1921	500,000,000
Nov., 1932	1924, 5% bonds at 10 years	30,000,000
Dec. 8, 1932	3, 6 and 10 year bonds, 1923 (1st series) repayable at 108%	Note (1)
June 27, 1933	3, 6 and 10 year bonds (Sept., 1923) repayable at 108%	Note (1)
Nov. 1, 1933	Credit National, 6%, 1921	500,000,000
Nov. 1933	1924, 5% bonds at 10 years	37,500,000
July 1, 1934	Credit National, 1922 (2d emission) repayable at 103	Note (1)
Nov. 1, 1934	Credit National, 6%, 1921	500,000,000
Nov., 1934	1924, 5% bonds at 10 years	7,263,558,750

In addition, 715 millions of sexennial loans must be repaid between August 16, 1925, and February 16, 1928. As their partition according to the date they fall due has not been published, it has been impossible to include them in the present table.

(Statement fixed upon according to the arrangements of the decrees of emission of the various loans).

(1) The amount of payment to be made cannot be fixed. It will depend upon the quantity of bonds which have been repaid at the previous periods when this same loan fell due.

ANNUAL COST OF THE COMMERCIAL DEBT

(In millions of gold francs)

<u>Year</u>	<u>Bank of England</u>	<u>American Stocks</u>	<u>Other Debts</u>	<u>Total</u>
1924	195	106	352	653
1925	219	106	330	655
1926	232	106	256	594
1927	246	106	193	545
1928	263	106	192	561
1929	403	2,223	217	2,843
1930	145	"	136	281
1931	"	"	120	120
1932	"	"	117	117
1933	"	"	113	113
1934	"	"	324	324
1935	"	"	107	107
1936	"	"	104	104
1937	"	"	101	101
1938	"	"	98	98
1939	"	"	108	108
1940	"	"	91	91
1941	"	"	384	384
1942	"	"	64	64
1943	"	"	61	61
1944	"	"	58	58
1945	"	"	55	55
1946	"	"	32	32
1947	"	"	30	30
1948	"	"	29	29
1949	"	"	27	27

(Figures given from information gathered (1) from the French and foreign press; (2) from the budget documents published since 1919, particularly:

The explanation of the reasons for the budget plan of 1923.

The inventory of the financial situation of France, 1924.

The parliamentary reports concerning the budget of the Ministry of Finance)

INHERITANCE TAXES

1

Rate of the Inheritance Tax (1)

<u>Amount</u> <u>of the Inheritance</u> Francs	<u>Three children</u> <u>living or rep-</u> <u>resented</u> %	<u>Two children</u> <u>living or</u> <u>represented</u> %	<u>One child</u> <u>living or</u> <u>represented</u> %	<u>No child</u> <u>alive or</u> <u>represented</u> %
2,000	0.30	0.60	1.20	3.60
10,000	0.54	1.08	2.16	6.48
50,000	0.83	1.66	3.31	9.94
100,000	1.01	2.03	4.06	12.17
250,000	1.31	2.61	5.22	15.67
500,000	1.55	3.41	6.51	18.63
1,000,000	2.13	4.25	8.06	21.92
2,000,000	2.98	5.73	11.23	25.32
5,000,000	3.79	7.15	14.21	25.58
10,000,000	4.29	8.08	16.11	32.79
50,000,000	5.08	9.54	19.06	38.44
100,000,000	5.42	10.17	20.33	40.82
500,000,000	6.36	11.63	23.27	43.68
1,000,000,000	7.68	13.02	24.23	45.24
Limit of the tax	9.	14.40	25.20	46.80

(1) Law of June 25, 1920 and March 22, 1924.

11 (1)

Transfer Duties

<u>Net amount</u> Francs	<u>From parents</u> %	<u>Between uncles</u> <u>and nephews</u> %	<u>Between relatives</u> <u>beyond the fourth</u> <u>degree and persons</u> <u>not related.</u> %
2,000	1.20	18	30
10,000	2.16	19.92	31.92
50,000	3.31	22.22	34.22
100,000	4.06	23.71	35.71
250,000	5.22	26.76	38.76
500,000	6.21	29.58	41.58
1,000,000	7.31	32.79	44.79
2,000,000	9.05	36.20	48.20
5,000,000	11.34	41.12	53.12
10,000,000	13.57	45.16	57.66
50,000,000	17.11	52.23	64.33
100,000,000	18.66	55.52	67.57
Limit of the tax	20.40	58.80	70.80

GENERAL TAX ON REVENUE

Revenue	Tax paid in 1925 (1) (Note is taken of the deduction of the tax of the preceding year)		Tax proposed for 1926 (2)	
	Amount	Per cent of revenue	Amount	Per cent of revenue
Fr.	Fr.	"	Fr.	"
7,000	"	"	"	"
20,000	328	1.64	299	1.50
30,000	779	2.60	759	2.53
40,000	1,435	3.58	1,419	3.50
50,000	2,277	4.55	2,279	4.56
100,000	8,960	8.96	9,579	9.58
200,000	29,422	14.71	27,961	13.98
300,000	54,335	18.11	53,436	17.81
400,000	83,028	20.76	86,411	21.60
500,000	114,957	22.99	126,886	25.38
600,000	149,259	24.86	162,452	27.08
700,000	185,086	26.44	200,242	28.61
800,000	222,060	27.76	241,032	30.13
900,000	259,560	28.84	284,822	31.65
1,000,000	297,060	29.71	331,612	33.16
1,500,000	484,560	32.30	610,562	40.70
2,000,000	672,660	33.60	876,920	43.85
3,000,000	1,047,060	34.90	1,316,920	43.90
4,000,000	1,422,060	35.55	1,756,920	43.92
5,000,000	1,797,060	35.94	2,196,920	43.94
10,000,000	3,672,060	36.72	4,396,920	43.97
Tax limit		37.50%		44%

The amount of the general tax on revenue is increased by 25% for taxpayers who are more than 30 years old and are bachelors or divorced and who, not having children, have no one dependent on them.

The same amount is increased by 10 per cent for taxpayers who are more than 30 years old and were married two years on the first of January of the imposition of tax, when, at that date, those taxpayers have no children and are found to have no person dependent upon them.

(1) Laws, June 25, 1920, March 30, 1923, and March 22, 1924.

(2) Project of law intended to create new fiscal resources, proposed on May 25, 1925.

COMPARISON OF THE GENERAL RATES OF TAXATION ON REVENUE AS APPLIED
IN FRANCE, IN ENGLAND AND IN THE U. S.

Revenues			France		England(3)	United States(4)
Frs.	L	\$	Rate		%	%
			Rate for 1925 (1)	Proposed for 1926 (2)		
			%	%		
7,000	70	350	---	---	---	---
20,000	200	1,000	1.64	1.50	---	---
30,000	300	1,500	2.60	2.53	---	---
40,000	400	2,000	3.58	3.50	---	---
50,000	500	2,500	4.55	4.56	---	---
100,000	1,000	5,000	8.96	9.58	---	---
200,000	2,000	10,000	14.71	13.98	---	---
300,000	3,000	15,000	18.11	17.81	2.92	0.40
400,000	4,000	20,000	20.76	21.60	5.31	1.10
500,000	5,000	25,000	22.99	25.36	7.25	2.04
600,000	6,000	30,000	24.86	27.08	8.96	3.07
700,000	7,000	35,000	26.44	28.61	10.54	4.09
800,000	8,000	40,000	27.76	30.13	12.03	5.10
900,000	9,000	45,000	28.84	31.65	13.47	6.07
1,000,000	10,000	50,000	29.71	33.16	14.62	7.08
1,500,000	15,000	75,000	32.30	40.70	18.08	12.12
2,000,000	20,000	100,000	33.60	43.85	19.81	17.02
3,000,000	30,000	150,000	34.90	43.90	22.38	23.68
4,000,000	40,000	200,000	35.55	43.92	24.28	27.01
5,000,000	50,000	250,000	35.94	43.94	25.42	29.21
10,000,000	100,000	500,000	36.72	43.97	27.71	34.
Limit of rate			37.50	44.	30.	40.

- (1) Account taken of the deduction of the taxes for the previous year.
 (2) Proposed law for the creation of new fiscal resources given in
 on May 25, 1925.
 (3) Finance Act, 1920.
 (4) Revenue Act, 1924.

(Laws of June 25, 1920, March 30, 1923, and March 22, 1924)

TAXES PAID BY A FRENCH BACHELOR MORE THAN 30 YEARS OLD

(Example)

A French bachelor, an industrialist on a small scale, having an income of 10,000 dollars (200,000 francs), coming, one-half from his business and the other half from personal property, paid in 1925:

	<u>Francs</u>
Taxes on industrial and commercial profits:	
9.60% on 100,000 francs	9,600
Tax on the income from personal property, 12% on 100,000 francs	12,000
Tax for the transmission of property to the bearer, (a tax that hits the coupon), 0.84% on the average rate on the stock exchange, say, 0.84% on 1,500,000 francs	12,600
General tax on net income of 165,800 francs	20,276
Surtax on bachelors: 25% of the general tax	5,069
	<hr/>
To wit, 29.77% of the total revenue	59,545

He will pay, in 1926:

A tax on industrial and commercial profits: 15% on 100,000 francs	15,000
A tax on the receipts from personal property 20% on 100,000 francs	20,000
Duty on the transmission of securities to the bearer,	12,600
General tax on a net revenue of 152,400 francs	18,470
Surtax on bachelors	4,618
	<hr/>
To wit, 35.34% of the total revenue	70,688

In the United States this taxpayer would only be subjected to the income tax, 6%. Not having an income above \$10,000 he would escape the super tax.

If he should die and leave his fortune to a nephew, the latter would pay, the inheritance tax being:

Value of the industrial capital,	1,000,000	francs
Personal property	1,500,000	"
Total	<hr/>	
Transfer tax	2,500,000	"
Inheritance tax	945,912	"
	669,168	"
	<hr/>	
To wit, 64.60% of the inheritance	1,615,080	"

If the heir was a relative beyond the fourth degree of the deceased, or had no relationship to him, the duties to be paid would be:

Transfer tax

The succession tax

To wit, 76.60% of the inheritance

1,245,912 francs

669,168 "

1,915,080 "

TAXES TO WHICH CORPORATIONS ARE SUBJECT

Transfer taxes on the cession of real property of commercial funds, and of credits, etc.
 Tax for registering judicial and extrajudicial acts (leases, contracts, etc.)
 Taxes on mortgages
 Tax on capital insured against fire
 Stamp duties on deeds and writings
 Stamp duties on posters
 Stamp duties on insurance contracts
 Stamp duties on transportation contracts
 Stamp duties on receipts, checks and transfers
 Stamp duties on commercial goods
 Stamp duties on personal securities (shares and loans put out by the corporation)
 Registration tax for trade marks
 Tax on the operations dealt in on the Stock Exchange
 Tax on the operations dealt in on commercial exchanges
 Tax on the revenue of the personal property possessed by the corporation
 Transfer taxes on the personal property possessed by the corporation
 Tax on the proceeds of credits, deposits and securities
 Tax on the amount of business
 Custom and export duties
 Taxes on statistics and on the development of external commerce
 Taxes on navigation
 Taxes on the cost of seats and of transportation by railroad
 Tax for transportation by other vehicles than railroads
 Tax on automobiles
 Taxes on verifying weights and measures
 Licenses for drinks and public vehicles
 Taxes on industrial and commercial profits
 Municipal and departmental taxes
 Tax on Chambers of Commerce

TAXES PAID BY THE SHAREHOLDERS

Tax on the income of personal property
 Tax on the transfer of personal property

TAXES PAID BY SHARE COMPANIES

(Example)

During the fiscal year from May 1, 1923, to April 30, 1924, which was nearly spent before the double tenth was established, the Sociéte des Acieries de Longwy (actual capital, 100 million francs) paid before any distribution:

Taxes and dues		8,008,422 francs	
It distributed among its shareholders		8,775,000	"
But these were obliged to pay to the Treasury as taxes imposed on their coupons		<u>3,436,670</u>	"
So that their revenue was reduced to		<u>5,338,330</u>	"
When the State had taken in:			
Taxes paid by the company:	8,008,422 francs		
Taxes paid by the share- holders	3,436,670	"	<u>11,445,092</u> "

We must add that the shareholders are besides subject to the progressive tax on their total income.

The example of the Longwy Steel Works is far from being singular.

At the coal mines of Blanzoy (capital 60 million francs) the taxes paid by the company and the shareholders, for the fiscal year 1924 amounted to 97% of the net revenue of the shares.

The mines of Lens (capital 200 million francs) paid directly in 1924:

		7,519,702 francs	
They shared among their shareholders		18,450,000	"
On which those had to pay to the State		<u>5,479,449</u>	"
Their revenue was, therefore, reduced to		<u>12,970,551</u>	"
The share of the State was:			
Taxes paid by the company:	7,519,702 francs		
Taxes paid by shareholders:	5,479,449	"	<u>12,999,151</u>

In 1926 the taxes paid by corporations will be notably increased for the tariff proposed for the tax on industrial and commercial profits which distinctly strikes all enterprises, is 15% instead of 9.60%, as it was in 1925, and the tax on the income from personal property will be raised from 12% to 20%.

After having paid the taxes to which it is subject, whether or not it obtains profits, a share corporation, in a position when it can declare a profit of:

	10,000,000 francs	
Must pay as a tax on industrial and commercial profits	<u>1,500,000</u>	"
On the profits thus reduced to:	8,500,000	"
The shareholders must pay:		
Tax on the income for personal property	1,700,000 Frs.	
Transfer tax (valuation)	1,000,000 "	<u>2,700,000</u> "
And will not receive more than	5,800,000	"

The State will take in the sum of 4,200,000 francs on the profits alone, independently of taxes imposed for various reasons, notably on the total amount of business in the course of the fiscal year.

G. Bendelari/E. Gross
Sept. 18, 1925