

The Papers of Charles Hamlin (mss24661)

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Hamlin, Charles S., Scrap Book – Volume 173, FRBoard Members

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FRBoard Members

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CONFIDENTIAL (F.R.)

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date July 17, 1941

To The Files

Subject: _____

From Mr. Coe

MRC.

After correspondence with Mrs. Hamlin (see letters of May 25 and June 4, 1941) the items attached hereto and listed below, because of their possible confidential character, were taken from Volume 173 of Mr. Hamlin's scrap book and placed in the Board's files:

VOLUME 173

Page 9

Letter to all F.R. Agents re Condition of Member Banks as of 6/30/27.

Page 33

Memo to Mr. Hamlin from Mr. Goldenweiser re Rate of bank expansion.

Page 59

Earnings and Expenses of F.R. Banks.

Page 133

Letter to Prof. Bullock, Harvard Economic Service, from F. H. Curtiss defending F.R. gold policy.

See Bk

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FEDERAL RESERVE BOARD

WASHINGTON

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

August 19, 1927
St. 5479.

SUBJECT: Condition of Member Banks
as of June 30, 1927.

Dear Sir:

For your information there is enclosed herewith a preliminary statement regarding the condition of all member banks combined as of June 30, 1927. The Board's Member Bank Call Report (No. 36) showing detailed figures for all member banks and for State bank members will be ready for distribution in the near future.

Very truly yours,

E. M. McClelland,
Assistant Secretary

VOLUME 173
PAGE 9

Enclosure.

LETTER TO ALL FEDERAL RESERVE AGENTS*

Loans and investments of all member banks on June 30 attained a new peak total of \$32,967,000,000, an increase of \$813,000,000 since March 23, the preceding call date. Central reserve city banks reported an increase of \$434,000,000 in loans and investments, reserve city banks an increase of \$120,000,000, and country banks of \$209,000,000. Loans and discounts including overdrafts totaled \$23,149,000,000, an increase of \$617,000,000 since March 23, and of \$882,000,000 since June 30, 1926. The principal changes in this item since March 23 were increases of \$436,000,000, \$134,000,000, and \$55,000,000 in the New York, Chicago, and Boston districts, respectively, and a decrease of \$19,000,000 in the Atlanta district. Investments in United States securities were \$40,000,000 less and in other securities \$236,000,000 more than on March 23, an increase of \$49,000,000 in security holdings being reported by banks in central reserve cities, of \$31,000,000 by banks in reserve cities, and \$116,000,000 by country banks.

Total deposits aggregated \$35,351,000,000, an increase of \$1,626,000,000 since March 23, and of a like amount since June 30, 1926. Demand deposits increased \$355,000,000 during the year, the principal increases being \$351,000,000 in the New York district and \$58,000,000 in the San Francisco district, while the Atlanta district reports the largest decrease, \$62,000,000. Time deposits increased \$1,037,000,000 since June 30, 1926, the principal increases by districts being New York - \$342,000,000, San Francisco - \$192,000,000, Philadelphia - \$103,000,000, Cleveland - \$97,000,000, Chicago - \$94,000,000, and Boston - \$88,000,000, while a nominal decrease was reported in one district, Minneapolis. Amounts due to banks and bankers were \$143,000,000 more than on June 30, 1926. The increase of \$1,626,000,000 in total deposits since March 23 is attributable in part to an increase in the amount of float carried by the member banks, uncollected items having increased \$757,000,000, of which \$590,000,000 was in exchanges for clearing house and checks on other banks in same place. Central reserve city banks in New York show an increase of \$1,066,000,000 in total deposits since March 23 and those in Chicago an increase of \$87,000,000, and reserve city and country banks of \$210,000,000 and \$263,000,000, respectively.

In the attached tables are figures by Federal reserve districts for all member banks and System figures for state bank members and for national banks.

Changes in the principal resources and liabilities as compared with figures for March 23, 1927, and June 30, 1926, were as follows:

		Increase (+) or decrease (-) since	
	June 30, 1927	Mar. 23, 1927	June 30, 1926
Loans & discounts (incl. overdrafts)	\$23,149,000,000	+\$617,000,000	+\$882,000,000
United States securities	3,795,000,000	- 40,000,000	+ 50,000,000
Other bonds, stocks and securities	6,023,000,000	+ 236,000,000	+ 644,000,000
Total loans and investments	32,967,000,000	+ 813,000,000	+1,576,000,000
Demand deposits	17,735,000,000	+*905,000,000	+ 355,000,000
Time deposits	12,210,000,000	+ 392,000,000	+1,037,000,000
Government deposits	218,000,000	- 189,000,000	- 10,000,000
Due to banks and bankers	4,124,000,000	+ 242,000,000	+ 143,000,000
Certified and cashiers' checks	1,065,000,000	+ 276,000,000	+ 102,000,000
Acceptances outstanding	536,000,000	+ 1,000,000	+ 68,000,000
Bills payable and rediscounts	541,000,000	- 5,000,000	- 71,000,000

*Demand deposits plus certified and cashiers' checks outstanding and less exchanges and other uncollected items increased \$423,000,000.

ALL MEMBER BANKS - CONDITION ON JUNE 30 AND MARCH 23, 1927

St. 5479b

RESOURCES	State Banks		National Banks	
	June 30	March 23	June 30	March 23
Loans and discounts (including overdrafts)	\$9,183,930,000	\$8,877,505,000	\$13,959,796,000	\$13,654,914,000
U. S. securities	1,202,328,000	1,185,952,000	2,593,114,000	2,642,199,000
Other bonds, stocks and securities	2,227,906,000	2,117,524,000	3,794,926,000	3,669,252,000
Total loans and investments	12,619,164,000	12,180,981,000	20,347,836,000	19,973,365,000
Cash in vault	174,699,000	165,475,000	363,157,000	372,830,000
Reserve with F. R. Banks	374,387,000	921,097,000	1,406,052,000	1,400,317,000
Items with Federal reserve banks in process of collection	243,900,000	230,367,000	496,916,000	443,145,000
Due from banks and bankers	499,282,000	478,146,000	1,469,044,000	1,418,237,000
Exchanges for clearing house, and checks on other banks in same place	864,123,000	521,760,000	1,048,819,000	700,910,000
All other resources	968,129,000	935,777,000	1,434,684,000	1,376,057,000
Total resources	16,243,684,000	15,433,603,000	26,566,508,000	25,684,861,000
LIABILITIES				
Demand deposits	6,818,585,000	6,406,070,000	10,916,659,000	10,424,639,000
Time deposits	4,896,689,000	4,763,589,000	7,313,145,000	7,054,105,000
U. S. deposits	79,693,000	167,764,000	137,929,000	239,086,000
Certified and cashiers' checks due to banks and bankers	525,800,000	386,406,000	538,805,000	402,116,000
Due to banks and bankers	1,267,980,000	1,100,988,000	2,855,673,000	2,780,427,000
Total deposits	13,588,747,000	12,824,817,000	21,762,211,000	20,900,373,000
Bills payable and rediscounts	173,206,000	147,390,000	368,042,000	399,043,000
Acceptances outstanding	267,100,000	274,698,000	268,537,000	259,901,000
Capital stock paid in	800,364,000	788,519,000	1,473,373,000	1,459,691,000
Surplus fund	774,252,000	753,214,000	1,256,090,000	1,238,960,000
All other liabilities	640,015,000	644,965,000	1,438,255,000	1,426,893,000

ALL MEMBER BANKS (7,790 NATIONAL BANKS AND 1,309 STATE BANKS) - CONDITION ON JUNE 30, 1927, BY FEDERAL RESERVE DISTRICTS
(In thousands of dollars)

St. 5479c

	Total	Federal Reserve District											
		Boston	New York	Phila- delphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
RESOURCES													
Loans and discounts	23,133,123	1,764,387	7,181,678	1,603,548	2,184,884	1,014,001	886,811	3,466,829	929,417	530,471	775,250	652,907	2,137,940
Overdrafts	15,603	594	2,913	626	966	429	1,402	1,975	1,456	596	850	1,198	2,598
U. S. Government securities	3,795,442	254,097	1,175,903	233,691	398,760	132,422	112,963	497,669	148,543	129,820	183,255	121,634	406,685
Other bonds, stocks and securities	6,022,832	537,622	1,923,823	692,909	689,780	164,794	142,651	753,677	257,841	190,508	194,154	55,150	419,923
Total loans and investments	32,967,000	2,556,700	10,284,317	2,535,774	3,274,390	1,311,646	1,143,827	4,720,150	1,337,257	851,395	1,153,509	830,889	2,967,146
Customers' liability on account of acceptances	502,024	44,808	369,416	14,806	7,039	4,969	10,290	20,057	836	671	315	2,488	26,329
Banking house, furniture, and fixtures	1,036,731	67,958	218,031	82,062	135,332	62,162	57,482	157,958	40,171	23,840	45,893	41,646	104,196
Other real estate owned	175,829	6,785	15,039	12,917	21,457	13,457	13,271	26,072	8,223	12,866	13,738	12,129	19,875
Cash in vault	537,856	40,041	122,145	42,808	57,154	27,569	26,128	83,621	21,950	18,724	27,276	22,107	48,333
Reserve with F. R. Banks	2,280,439	149,723	918,169	140,900	180,034	73,254	65,820	310,885	77,050	47,781	90,771	62,028	164,024
Items with F. R. banks in process of collection	740,816	65,563	262,022	58,034	69,351	40,895	23,955	82,445	34,433	8,013	36,916	23,458	35,731
Due from banks, bankers, and trust companies	1,968,326	103,185	227,765	112,284	168,759	104,877	136,702	336,691	111,535	105,616	200,021	130,524	230,367
Exchanges for clearing house, and checks on other banks in same place	1,912,942	60,273	1,453,980	59,831	46,812	26,253	20,881	121,291	20,424	9,143	21,335	11,232	61,487
Outside checks and other cash items	177,771	8,088	44,002	3,892	10,366	5,148	7,287	39,550	3,637	7,818	5,022	3,762	39,199
Redemption fund and due from U. S. Treasurer	32,891	2,331	4,257	2,848	4,107	3,000	1,995	4,226	2,020	1,390	1,704	2,317	2,696
U. S. securities borrowed	27,243	108	181	1,142	8,486	2,000	2,134	5,141	4,827	122	474	396	2,232
Other securities borrowed	6,296	21	805	100	590	125	1,401	2,331	24	5	252	102	540
Other assets	444,028	34,716	261,509	14,291	18,265	4,695	7,981	46,280	13,257	4,404	4,025	2,644	31,961
TOTAL	42,810,192	3,140,300	14,161,638	3,081,689	4,002,142	1,680,050	1,519,154	5,956,698	1,675,644	1,091,788	1,601,251	1,145,722	3,734,116

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ALL MEMBER BANKS (7,790 NATIONAL BANKS AND 1,309 STATE BANKS) - CONDITION ON JUNE 30, 1927, BY FEDERAL RESERVE DISTRICTS
(Amounts in thousands of dollars)

St. 5479d

	Total	Federal Reserve District											
		Boston	New York	Phila- delphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minn- neapolis	Kansas City	Dallas	San Francisco
LIABILITIES													
Capital stock paid in	2,273,737	165,482	633,280	160,893	216,675	117,230	100,460	318,924	114,430	63,355	93,508	95,107	194,393
Surplus fund	2,030,342	147,630	664,928	276,934	243,387	88,012	67,731	254,030	61,417	33,925	43,027	43,707	105,614
Undivided profits, less expenses and taxes paid	843,319	76,830	303,800	82,328	79,503	32,107	24,046	106,514	29,570	15,087	18,767	22,541	52,226
Reserved for taxes, interest, etc., accrued	128,142	14,433	41,700	7,257	11,559	4,592	4,336	24,314	3,713	4,189	3,079	2,472	6,498
Due to F. R. banks	53,043	6,981	17,543	7,214	4,151	9,695	2,191	2,870	307	-	134	1,525	432
Due to banks, bankers, and trust companies	4,070,610	187,263	1,698,404	201,875	251,045	128,860	148,254	570,191	171,651	98,500	235,840	116,303	262,424
Certified and cashiers' or treas- urers' checks outstanding	1,064,605	26,391	806,817	19,072	24,294	12,562	9,624	53,173	12,880	9,813	19,378	12,812	57,789
Demand deposits	17,735,244	1,375,920	6,476,620	1,141,007	1,461,849	600,893	577,982	2,355,202	657,482	391,293	800,373	535,625	1,300,993
Time deposits	12,209,834	932,343	2,654,557	1,000,432	1,523,854	566,449	461,993	2,029,289	509,282	434,987	331,110	180,830	1,584,708
United States deposits	217,622	23,936	32,922	25,778	21,243	12,922	16,844	23,968	6,981	5,693	7,038	10,972	29,325
Total deposits	35,350,958	2,552,834	11,686,863	2,395,378	3,286,436	1,331,381	1,216,888	5,034,693	1,358,583	940,286	1,393,873	918,067	3,235,676
Agreements to repurchase U. S. Govt. or other securities sold	17,967	954	10,289	3,638	545	571	21	70	79	25	40	1,580	155
Bills payable	381,133	39,045	99,310	53,091	42,520	21,436	19,060	39,765	24,525	1,694	1,500	8,013	31,174
Notes & bills rediscounted	160,115	21,439	13,250	12,640	5,991	14,043	23,435	28,649	13,928	3,372	10,392	3,500	9,476
Acceptances of other banks and foreign bills of exchange or drafts sold with indorsement	210,519	21,033	158,513	4,694	7,325	820	2,731	8,216	506	13	-	33	6,635
Letters of credit & trav. checks sold for cash and outstanding	41,696	1,037	30,668	600	4,028	141	218	3,607	195	17	131	127	927
Acceptances executed for customers	503,595	45,482	366,576	12,339	6,949	6,237	12,922	20,611	845	684	315	2,480	28,155
Acceptances executed by other banks for account of reporting banks	32,042	1,805	23,471	3,384	366	234	704	606	-	60	-	-	1,412
National-bank notes outstanding	650,445	46,070	84,206	55,956	80,993	58,477	39,494	84,293	40,074	27,582	33,930	45,880	53,490
United States securities borrowed	27,268	108	181	1,142	8,486	2,025	2,134	5,141	4,827	122	474	396	2,232
Other securities borrowed	6,296	21	805	100	590	125	1,401	2,331	24	5	252	102	540
Other liabilities	152,618	6,097	63,798	11,315	6,789	2,619	3,573	24,934	22,928	1,372	1,963	1,717	5,513
TOTAL	42,810,192	3,140,300	14,181,638	3,081,689	4,002,142	1,680,050	1,519,154	5,956,698	1,675,644	1,091,788	1,601,251	1,145,722	3,734,116
Number of banks	9,099	414	927	773	841	569	469	1,308	599	740	972	815	672

W.

Office Correspondence

FEDERAL RESERVE
BOARD

Date August 30, 1927

To Mr. Hamlin

Subject:

From Mr. Goldenweiser

Rate of bank expansion

See App
Page 33*E. G. G.*

2-5495

In compliance with your recent request, I am submitting the following explanation of the manner in which the expansion of credit based on a given amount of additional reserves spreads itself through the banking system. In the example it has been assumed that the banks involved all operate under the 10 per cent reserve requirement. Any other percentage would be just as good, except that 10 per cent makes the arithmetic easier. It is understood that the facts presented refer simply to the course of events arising out of one circumstance, namely, the deposit of \$1,000,000 of gold. In reality there will be a number of other transactions occurring from day to day, and this would conceal the workings of the one factor here under discussion.

Assume that Bank A receives a deposit of \$1,000,000 in gold. This would increase its deposit liabilities by \$1,000,000 and when it passes the gold on to the reserve bank, as it always does, it will place \$1,000,000 of reserve bank funds at its disposal. Of this \$1,000,000, however, \$100,000 will have to be retained as reserve against the additional million of deposits, and, therefore, the free balance at the disposal of the bank will amount to \$900,000. This amount Bank A will lend to some one, and we will assume that this some one, whom we shall call X, will purchase something from Y and draw a check for the amount borrowed in favor of Y, who is a depositor in Bank B. Bank B, therefore, will receive a deposit of \$900,000 in reserve funds which will increase its deposit liabilities by this amount and its reserve requirements by \$90,000, leaving \$810,000 as a free balance available for loaning or investing. Assume that Bank B uses this balance of \$810,000 to buy Government securities from Mr. Z, paying him with a check. Now, Mr. Z, being a depositor in Bank C, will take the check

Office Correspondence

FEDERAL RESERVE
BOARD

Date _____

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To _____

Subject: _____

From _____

2-8495

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to his bank and deposit it to his own credit. Bank B would then lose \$810,000 through the clearing house to Bank C, and Bank C would obtain \$810,000 of Federal reserve bank funds. The liabilities of Bank C on deposits would increase by \$810,000, which would increase its reserve requirements by \$81,000, leaving a balance of available funds of \$729,000. These transactions will continue so long as there are free funds available, and this will be until the total volume of additional deposits amounts to \$10,000,000 and the entire \$1,000,000 of funds arising from the gold deposit will thus be required to support these additional deposits, so that there will be no free balance. The table illustrates the

transactions:

	<u>Increase in deposits</u>	<u>Increase in required reserve</u>	<u>Free balance</u>
Bank A	\$1,000,000	\$100,000	\$900,000
B	900,000	90,000	810,000
C	810,000	81,000	729,000
D	729,000	72,900	656,000
Etc.			
Total	10,000,000	1,000,000	-

It will be seen, therefore, that while no individual bank can lend more funds than it has at its disposal, because it would lose the money through the clearing house, and would not be in a position to meet its adverse clearing house balance, the reserve funds arising from a gold deposit are passed around from bank to bank until the member banks' deposits based on it have reached the maximum permitted by law. It does not make any difference how many banks are involved. Each new step in the transaction is marked by a new deposit, which may be made in the same bank or in another bank. In either case the new deposit increases the bank's liability by the amount deposited and increases the funds at its disposal for lending or investing by the same amount, less the required 10 per cent reserve.

This assumes that original and copies deposited do not claim themselves checked as 1/10/11.

EARNINGS AND EXPENSES OF FEDERAL RESERVE BANKS

AUGUST 1927. Total earnings of the Federal reserve banks were \$16,000 more than in July, a decrease of \$201,000 in earnings from discounted bills being more than offset by increases of \$63,000 in earnings from purchased bills and U. S. securities and of \$154,000 in miscellaneous earnings. The increase in miscellaneous earnings was due to an increase in the amount of interest earned on balances held abroad and to profits on securities sold.

Current expenses (exclusive of cost of Federal reserve currency) aggregated \$2,167,000 as compared with \$2,144,000 in the month preceding and \$2,139,000 in August 1926.

EIGHT MONTHS ENDING AUGUST 31, 1927. During the eight months ending August 31 earnings totaled \$27,352,000, as compared with \$30,467,000 for the corresponding period last year and \$25,776,000 for 1925.

Current expenses (exclusive of cost of Federal reserve currency) amounted to \$17,184,000 during the eight-month period, an increase of \$68,000 over the corresponding period last year.

After providing for all current expense and dividend requirements, the Federal reserve banks on August 31 had a balance of \$3,810,000 available for depreciation allowances, surplus and franchise taxes, as compared with a balance of \$7,352,000 at the end of August 1926.

On June 30 earnings of the Federal Reserve Bank of Richmond were \$59,500 less than expense and dividend requirements, but this deficit was reduced to \$38,800 on July 31 and now amounts to only \$7,600.

CONFIDENTIAL

Not for publication

EARNINGS AND EXPENSES OF FEDERAL RESERVE BANKS, AUGUST 1927.

St. 5499

Federal Reserve Bank	Month of August 1927						Year 1927					
	Earnings				Current expenses		Current net earnings	Annual rate of current net earnings on average paid-in capital	Current net earnings to Aug. 31	Dividends accrued to Aug. 31	Balance available for depreciation allowances, surplus, franchise tax, etc.	
	From dis-counted bills	From pur-chased bills and U. S. securities	From other sources	Total	Exclusive of cost of currency	Total					On Aug. 31	On July 31
							Per cent					
Boston	\$98,368	\$99,280	\$20,521	\$218,669	\$150,453	\$167,997	\$50,672	6.3	\$519,641	\$361,799	\$157,842	\$155,878
New York	366,951	419,898	77,876	864,725	502,108	542,812	321,913	9.7	2,067,395	1,530,418	536,977	410,778
Philadelphia	135,628	110,246	23,794	269,668	161,608	175,035	94,633	8.5	710,305	516,700	193,605	164,607
Cleveland	88,797	179,525	35,210	303,532	195,062	217,408	86,124	7.3	1,008,077	553,567	454,510	440,249
Richmond	65,443	86,219	18,048	169,710	104,816	107,397	62,313	11.8	239,648	247,222	*7,574	*38,772
Atlanta	115,359	60,131	18,430	193,920	95,356	96,289	97,631	22.3	588,865	203,022	385,843	313,939
Chicago	139,807	258,864	71,705	470,376	332,144	346,878	123,498	8.4	1,388,599	681,566	707,033	670,078
St. Louis	80,362	102,581	14,273	197,216	110,381	112,859	84,357	18.8	580,083	211,429	368,654	310,736
Minneapolis	20,866	74,828	10,760	106,454	82,668	86,616	19,838	7.8	167,855	120,556	47,299	42,974
Kansas City	32,428	112,175	34,659	179,262	134,816	135,610	43,652	12.2	377,950	168,209	209,741	187,197
Dallas	41,927	99,961	13,808	155,696	105,343	115,339	40,357	11.1	249,935	170,806	79,129	60,082
San Francisco	157,107	162,712	28,798	348,617	192,010	216,102	132,515	17.0	1,037,985	361,127	676,858	590,339
TOTAL:												
Aug. 1927	1,343,543	1,766,420	367,882	3,477,845	2,166,765	2,320,342	1,157,503	10.5	8,936,338	5,126,421	3,809,917	3,308,085
July 1927	1,544,557	1,703,382	213,849	3,461,788	2,143,978	2,282,969	1,178,819	10.7				
Aug. 1926	1,845,971	1,748,712	206,632	3,801,315	2,139,328	2,279,768	1,521,547	14.5	12,196,068	4,843,770	7,352,298	6,446,945

FEDERAL RESERVE BOARD

DIVISION OF BANK OPERATIONS

SEPTEMBER 12, 1927.

C.

*Deficit.

FEDERAL RESERVE BANK OF BOSTON
30 PEARL STREET

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September 1, 1927.

Professor C. J. Bullock,
c/o Harvard Economic Service,
Harvard Square,
Cambridge, Mass.

Dear Charles:

The Harvard Economic Service letter of July 23 which you sent to me at Bar Harbor was received and read with greatest interest. I like the presentation of the picture of the United States as a creditor nation and of the world gold stocks and gold imports into the United States, and also the one on the gold situation and world prices.

I do not, however, agree with you and with Professor Sprague in the use of the term "sterilizing", or the burying of gold by the Federal Reserve System, and the analogy of the policy of the Federal Reserve System with the "historic rôle that has been played by India". I think there is every evidence that the gold that has come into this country during the period in question has "fermented" and has had a marked influence on our credit structure. It seems to me that there are five ways in which gold could come to this country; first, as a deposit with the Federal Reserve Bank; second, as a deposit with a private bank; third, as received in payment of goods; fourth, being sent to a Federal Reserve Bank or to a private bank for reinvestment; and fifth, where the gold is sent for safe keeping and earmarked by a Federal Reserve Bank. Of these methods the only two that would appear to me to sterilize the gold would be where it was placed on deposit with a Federal Reserve Bank and not reinvested by the Federal Reserve Bank, or when the actual gold was sent for safe keeping and earmarked, and as this latter transaction does not appear in the Reserve Banks' figures it need not be considered. So far as I am able to learn, very little gold, if any, has come as a straight deposit to the Federal Reserve Bank from Europe and practically all has come either in payment of goods, as a deposit with private banks, or to the Reserve Bank, or other banks, for reinvestment.

The period in question I take to be the years 1921 to date. During that time the stock of gold in the United States rose from three billion to something over four billions and a half. During that same period the total loans and investments of the member banks alone rose from about twenty three billions to about thirty three billions, which does not include real estate owned in the form of bank buildings. While I appreciate that a part of this increase in loans and investments has come from the large increase in time deposits which allow for larger loan expansion owing to their low reserve, I am led to believe that a large portion of the time deposits are really demand deposits, but nevertheless this expansion during that period certainly must be due to the large

FEDERAL RESERVE BANK OF BOSTON
30 PEARL STREET

Professor C. J. Bullock

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September 1, 1927.

increase in gold during that period. You do not seem to allow at all for this expansion in any of your discussions. Inasmuch as comparatively low rediscount rates had been maintained during that period by all Reserve Banks and all credit asked for by the member banks and bill market has been supplied, the only other method of putting this gold to further use would have been for the Federal Reserve Banks to have bought all of the bankers' acceptances offered on the market and a large volume of government securities, i.e. to have released to the market additional credit of approximately a billion and a half which would have allowed the member banks to have increased their loans and investments to many times that amount. That there has been during this period an excess of credit for normal use by the banks is evidenced by the poorer grade of securities and real estate mortgages which have been coming into their portfolios particular with the fall of money rates.

I am still very much confused and have heard no adequate explanation of the fall of commodity prices. The wholesale commodity price index of the United States Bureau of Labor Statistics shows a steady increase in prices from early in 1922 until the spring of 1923 and although the effect of the increase of discount rates in the spring of 1923 I know you feel started a downward movement in commodity prices, these were checked in the summer of 1924 and in 1925 against went to a new high peak which continued through that year. At that time the rates were dropped to $3\frac{1}{2}\%$, and were continued there during 1924 and 1925, and even to 3% in the case of New York, and since that time have been maintaining at the same or lower rates than occurred during the periods of 1921 and 1923. I am led to the conclusion, therefore, that there are some other factors working on commodity prices which we have not yet discovered, that have brought about conditions from 1925 on and which are not traceable to the policy of the Federal Reserve Banks. I should like to discuss this with you further when the opportunity arises.

I have not written you before regarding this matter as you have been in the West since my return and are only returning tomorrow morning.

Trusting you are well, and with kindest regards, I am

Sincerely yours,

(Frederic H. Curtiss)

P.S. Since writing the above, I have seen an article in the Wall Street Journal which points out that certain of the central banks of Europe are counting their balances in this country as reserve. Does this mean that there has been expansion in Europe on these balances?

COPY

Charles J. Bullock, Chairman.

HARVARD UNIVERSITY
Committee on Economic Research
Cambridge, Mass.

September 3, 1927.

Mr. Frederic H. Curtiss,
Federal Reserve Bank of Boston,
30 Pearl Street,
Boston, Mass.

My dear Fred:

Your letter of September 1 reached me yesterday. I had no idea that you were back in these parts, or I should have dropped in to see you Thursday, when I was in Boston. Mrs. Bullock and I got back from Canada Wednesday night; and I went into Boston Thursday morning to attend to a number of items of business.

In regard to your letter, it seems to me that you have not quite "got" when we said about "sterilizing" imported gold. We did not argue that this gold had had no effect upon our credit structure, but said merely that, so far as commodity prices were concerned, the gold had been "sterilized". On page 191, indeed, we said that considerable expansion of credit had occurred and could not possibly be prevented, as security markets and the construction industry showed. We merely said that, "in commodity markets", the imported gold produced little effect. I fully agree with all that you say about the way the gold has expanded credit in various directions other than commodity prices.

I also agree that there are some other factors beside federal reserve policy that have been operative; and we will talk these over next week, when I hope to see you.

We have had a good trip; and I shall hope to hear that you and Mrs. Curtiss had a fine vacation also.

Yours sincerely,

C.J.B.

THE FUTURE OF THE WORLD PRICE LEVEL

By Professor Bertil Ohlin.

THE FUTURE OF THE WORLD PRICE LEVEL

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I.

The experiences of the past twelve years in the monetary sphere have demonstrated very clearly - painfully clearly, in fact - the significance of stable price conditions. The question of a stabilization of the price level is one of undiminished urgency, in spite of the fact that the violent price fluctuations experienced during the paper-standard régime of the past decade have now become impossible in most countries as a result of their currencies being bound to gold. For there still remains a problem of fundamental, though less striking, importance, namely, how to achieve a stabilization of the intrinsic value of gold and thereby of the world price level.

The discussion on this question began, long before the Great War, during the long period of inflation that lasted from 1895 to 1913. The debate has now been resumed along practically the same lines as before. The report of the Indian Currency Commission contains weighty contributions to the subject. More recently, the Midland Bank's monthly review and Professor Cassel's article in the Skandinaviska Kreditaktiebolaget's quarterly review have subjected the factors determining the future value of gold to an interesting analysis.

Generally an enquiry into the causes of variations in the value of gold before the war proceeds along some such lines as the following: The volume of gold production is placed in relation to the demand for fresh gold on the part of the monetary system on the one hand, and on the part of industry and "hoarding" on the other. At periods when the former

exceeded the sum of the two latter, gold dropped in value and the price level rose - which occurred as a result of the discovery of the great goldmines in the 'fifties and after the rapid growth of gold production towards the end of the 'nineties and the beginning of the present century. Between these two periods of falling gold-values occurred a period of deflation during the years 1875-95. An unusually keen demand for gold, which was chiefly due to a number of countries adopting the gold standard at a time when gold production was comparatively small, resulted in an increase in the value of gold.

In the light of more recent experiences, however, these fluctuations in the world price level - 20 - 30% in the course of some twenty years - appear fairly modest. We are at once forced to seek an explanation as to why the gold value before the war was as constant as it actually was, while the value of other commodities was subject to both wider and, above all, more violent fluctuations. A discussion of this problem is all the more interesting because it provides a good background for the discussion of the urgent problem as to how we are to achieve and to guarantee a still more complete stabilization of the value of gold in the future.

Gold production varied very considerably during the last century, as will be seen from the following average figures for the respective periods:

The world's production of gold (in mill. £ Sterling):

1835-39..2.8	1865-69..26.8	1895-99..50.6	1920-24..70.8
1845-49..7.6	1875-79..22.4	1905-09..86.2	
1855-59.27.6	1885-89..22.8	1915-19..86.0	

One would think that it was more by a lucky chance than anything else that such an extraordinary rise in the supply did not cause still

wider fluctuations in the value of gold than those which the world experienced. True, the demand for gold, both for industrial and monetary purposes, grew, but there is no reason for its fluctuating in accordance with the gold production.

Let us first of all examine the demand for monetary purposes. Most countries having introduced the gold standard in the 'seventies, the demand was determined primarily by the increased need for means of payment which was the result of the growth of population and production and of the transition to a complete monetary economy. On the other hand, the growing use of various forms of credit naturally entailed a corresponding decrease in the need for money - gold currency and notes issued on a gold basis.

The industrial demand seems to have shown a fairly steady increase, but nothing is known for certain on this point. This applies still more to the demand on the part of India and China for hoarding purposes - a factor which in times of prosperity exercised considerable influence in those countries. It has been estimated that nearly 40% of the world's gold production disappeared in Indian and Chinese hiding-places during the years 1924-26. f

The fact that under the influence of these factors, which apparently are mutually independent, the value of gold maintained a comparatively high degree of stability before the war clearly needs a specific explanation. This can only be found in the nature of the monetary demand.

The monetary system of the world does not "consume" gold in the same way as industry. Bullion merely accumulates in the vaults of the banks or is minted and put into circulation. The annual gold-produc-

tion - or rather, that part of it which the monetary system obtains when industry and hoarders have taken their portion - is comparatively small in relation to the reserves thus amassed.

While before the war the annual addition to these stocks of gold was something like £ 50 mill., the stocks amounted to about £ 1.500 mill. These large reserves form a powerful means of preventing violent fluctuations in the value of gold.

This is best illustrated by an imaginary example, which however practically has its counterpart in reality. Let us assume that during a certain period an annual addition to the gold stocks of about £ 30 mil. was found necessary in order to keep the gold value stabilized, owing to the increasing production and trade, in spite of the economy effected by credits. Suppose, further, that the gold production and the demand on the part of industry and hoarders varied, with the result that in some years £ 50 mill. of fresh gold was at the disposal of the monetary system, while for a year or two afterwards the annual addition remained at £10 mil.

If the demand for gold were of the same nature as that for other commodities, such fluctuations in the supply could not have failed to entail very wide fluctuations in value. It is obvious, however, that the large gold reserves exercise a stabilizing influence.

If the additional supply of fresh gold in any given year exceeds requirements for the maintenance of a stabilized price level, the latter naturally shows a tendency to rise. This increases the requirements for means of payment, notes and gold coin. Both the banks and the Mint must necessarily increase their demand for gold, which naturally tends to prevent the fall in value that would otherwise have resulted from the excessive supply. If the latter during a period of three years exceeded

by, say, £ 20 mill. what was required for a stabilized price level, this would merely mean that the world's gold reserves were 4% too high (£ 60 mill, too high is 4% of 1.500), the result of which, other conditions being equal (constant percentage of cover for notes and unvarying monetary habits on the part of the population) would be a rise in prices on approximately the same scale. In other words, the value of gold has fallen by only 4%, in spite of the supply of gold for monetary purposes having exceeded the size of the demand, taking the gold value as constant, by 67% (£ 50 mill. instead of 30 mill.).

This we may express by saying that the demand for gold for monetary purposes possesses very great elasticity: even a slight drop in value at once results in a strong increase in the demand for fresh gold. The opposite argument of course holds good in the case of an inadequate provision of fresh gold for monetary purposes.

The large gold reserves constitute a reservoir which can take in or deliver considerable quantities of gold without any appreciable effect on the surface-level - the gold-value.

There is no reason to suppose that the demand for gold for industrial or hoarding purposes possesses any marked degree of elasticity. If gold were demonetized and became a commodity like any other, the variations in gold-production and in demand would doubtless lead to very heavy fluctuations in the value of gold.

From this it would appear that during the last half-century before the Great War the stability of the gold-value had nothing to do with the quality of gold as a commodity, but was due exclusively to the nature of the monetary demand. The decisive factor, in other words, was the organization of the monetary system, above all a certain conservatism

in the practice of the central banks in regard to gold-cover and in the general public's habits of payment.

During the war the correctness of this view received a confirmation which was as complete as it was surprising. Changes of various kinds in the monetary system, which it is not necessary to describe here in detail as they are still fresh in the memory, brought about a rise in the price level, even in countries with a gold standard, to a height which was more than double the pre-war level. The value of gold in relation to commodities thus fell to less than half of what it was in 1913. What, then, became of the intrinsic stability of the gold-value, which had so often been declared to be the reason for its suitability as a basis for the monetary system? A change in the organization of the monetary system was sufficient to cause a veritable bouncing up and down of the value of that commodity.

The points thus indicated will suffice to show that the value of gold is a question of the organization of the monetary system and nothing else.

II.

If we are to consider what prospects exist for the future stability of the world price level and the value of gold, the first thing to do is clearly to examine how far the monetary system, as it appears today after the return to the gold standard, differs from the special kind of gold standard that prevailed before the war.

Perhaps the most striking change is that in most countries gold coin has disappeared from circulation. It is estimated that about £ 500 mill. were in circulation before the war, whereas now four-fifths of that amount have been withdrawn and lie in the vaults of the central

banks. The correspondent strengthening of the gold reserves has made it possible to maintain practically the same regulations for covering the note-issues as before the war, in spite of the world price level being now about 50% higher than it was then, with the result that there is a proportionately increased need for means of payment.

This change however, once effected, produces no essential alteration in the character of the gold standard. A rise in the gold value, i.e., a fall in the general price level, results in a reduction in the banks' gold-cover requirements for a diminished quantity of notes. This causes a reduction in the demand for the newly-produced gold, which fact tends to lower its value or at any rate to counteract a further rise.

So long as the banks adhere to their pre-war practice in regard to the note-cover, and the general public's habits of payment do not undergo any violent change, the monetary demand for gold will have the same elasticity and stabilized character as it had formerly.

On the whole it may be said that no very important change has taken place in either respect. It would appear, however, as if the belief in the advantage of large gold stocks had grown during the past decade, and as if for that reason a reduction in the stock of notes is in many cases not accompanied by a diminution of the gold reserves. In fact, the rise in the percentage of cover that takes place instead is regarded as a sign of strength.

Should such a practice become widespread, it is bound in the long run to have very serious consequences. The tendency for the gold demand to fall off - the usual result of a rise in the gold value, i.e., a falling price level and a shrinking note issue - would disappear.

A considerable rise in the value of gold and a serious drop in the world price level would then be far more likely than before.

We see, then, that the semi-automatic regulation of the monetary value that prevailed before the war is in danger of undergoing a decided change for the worse if the former note-cover practice is altered.

Of far greater importance to the monetary system than the change that may already have taken place in this respect is, however, the redistribution of the world's gold stocks. The United States have become the possessors of a quantity of gold - in fact, considerably more than half of the gold stocks in the world - by no means proportionate to what is required to cover their circulating medium. Simultaneously with this accumulation of gold a significant reform has taken place in America's monetary policy. In order to prevent this vast influx of gold from causing a corresponding expansion of credit, which would necessarily involve a violent inflation, the Federal Reserve Board has been compelled entirely to disregard the size of the gold reserves in determining the question of credit.

The influx and efflux of gold in the United States has thus lost all influence upon the monetary purchasing power and the price level in that country. The question of granting credit is instead determined by what the Federal Reserve Board considers suitable from an economic **point of view**.

This implies nothing less than a revolution in the monetary system not only of the United States but of all countries with a gold standard. The control of the development of the world price level has passed entirely into the hands of the Federal Reserve Board and Governors.

Should that Board deem it advisable to pursue a liberal credit policy, resulting in the raising of the American price level, the consequence would be that a portion of the superfluous gold would flow to other countries. There it would cause an expansion of credit and gradually a raising of the price level all along the line.

If, on the other hand, it is considered in the United States that a reduction in prices would be advisable, then other countries are compelled to follow suit. Otherwise their price level would eventually be too high, their balance of payment would become "adverse" and their gold would begin flowing into the vaults of the Federal Reserve banks. This the European central banks cannot, in view of their note-cover, permit, but are forced to carry out a restrictive credit policy that rapidly reduces the price level in Europe as well.

Other countries are thus compelled to let their price level vary on about the same lines as the American. If the Federal Reserve Board resolves upon raising the value of gold, i.e., upon deflation, then its reserves increase, while, vice versa, a lowering of the gold value in the United States can be forced upon the whole world in connection with a reduction in the excessive gold reserves of the Federal Reserve system.

The Federal Reserve system has effected a "valorization" of gold, comparable to the Brazilian coffee valorization. By releasing a portion of the surplus reserves it causes a drop in the gold value throughout the world - i.e., a rise in the world price level. By increasing the reserves it brings about an increase in the scarcity of gold and a fall in the world price level.

It should however be observed that the primary change is always a variation in the American price level. The resultant increase or reduction in gold stocks is something secondary, something that is permitted to take place in order that the national monetary policy may not be disturbed by the movements of gold which under present circumstances are of no very great concern to the United States.

We find a recent example of this in the last two years' fall in prices, both in America and Europe. During this period, the United States, after some exportation of gold in 1925, have been importing gold in quite considerable quantities. No greater mistake could be made than to regard this general deflation of prices as a result of a reawakened desire for gold on the part of America. What possible reason would the Federal Reserve Board have for increasing their already inconveniently large gold stocks? The real reason, on the contrary, is that the price level in the United States has been dropping - partly, no doubt, owing to an insufficiently liberal credit policy, and partly owing to heavy crops and increased industrial productivity - and that other countries have reluctantly followed suit in this fall in prices, their central banks being forced by the threatening efflux of gold to adopt a restrictive credit policy.

III.

The result of the present enquiry is, primarily, this: 1) The pre-war gold standard was in reality an example of "managed currency", in which the control acquired a semi-automatic character because the central banks were all actuated by practically similar traditional principles of credit policy, gold cover, etc., and because the public habits of payment underwent no violent changes; 2) The post-war gold standard is an entirely

different kind of "managed currency", in which the control is exercised by the Federal Reserve Board and the boards of the leading Federal Reserve Banks on the basis of considerations which have nothing to do with either gold cover or gold movement, but are chiefly dictated by the possibilities of keeping production going at full pressure.

One can hardly avoid a third conclusion - that no enquiries into the probable extent of the gold production and demand are of much use for determining the course of prices during the next ten years. Variations in these factors are not likely to induce the Federal Reserve Board to abandon its present policy, but will only lead to either an increase or a reduction in the quantity of gold stagnating in the vaults. As regards the course of prices later on, it is possible that the Federal Reserve System's reserves will not prove sufficient to cope with the forces emanating from fluctuations in the gold production and demand. To estimate the strength of these forces after 10 years or so is, however, at present only possible with such wide margins of uncertainty that the conclusions can hardly as yet evoke much interest.

The development of the world price level during the next decade is a question of American monetary policy. The decision regarding its stabilization lies in the hands of the leaders of that policy. It is a tremendous responsibility. A real deflation would render Europe's economic recovery, if anything, still more difficult. It may well be asked whether the Federal Reserve Board is not partly responsible for the tardy improvement of the past few years. This question - to what extent the fall in prices during 1926 and 1927 can be regarded as a deflation likely to result in economic depression - must, however, be made the subject of a separate analysis.
