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Form F. R. 131

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date August 12, 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 267 of Mr. Hamlin's scrap book and placed in the Board's files:

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Page 19
International Gold and Capital Movements.

Page 50
Letter from Mr. Goldenweiser attaching memo summarizing data re reserve requirements of member banks.

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

Highly Confidential

October 21, 1935

INTERNATIONAL GOLD AND CAPITAL MOVEMENTS

The current movement of gold from Europe to the United States began early in September with small shipments from London. On September 17 the first gold arrived from France, and on September 23 shipments were received from the Netherlands. In the five weeks ending October 21 about $370,000,000 of gold arrived in the United States, and $50,000,000 more is scheduled to arrive during the next ten days. Of this $420,000,000 France has shipped $195,000,000, England $125,000,000 and the Netherlands $55,000,000. The remainder has come largely from India and Canada.

This heavy movement of gold does not reflect an excess of payments due to the United States on ordinary transactions with the world. Recently this country's merchandise exports have exceeded its imports by only a small amount. Largely because of agricultural developments the surplus of exports has been cut down from an average of $32,000,000 a month for the first eight months of 1934 to less than $4,000,000 a month in 1935. This small excess, together with income from foreign investments, has been more than balanced in 1935 by tourist expenditures abroad, immigrants' remittances, and freight payments to foreign vessels. That gold nevertheless has flowed to the United States during the year is attributable to the heavy movement of capital to this country. The volume of gold imports has been held below the inward movement of capital by purchases of silver abroad for account of the United States Treasury.

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During the crisis in the gold bloc countries last spring, the movement of capital was largely in the form of short-term balances. Speculative and flight funds were being transferred from these countries to New York. There was also a large return of New York funds from London, where the discount on forward sterling made the continued holding of balances unprofitable. During the summer forward quotations on sterling and gold bloc currencies continued to be at a discount, and there was little return to Europe of funds that had come here in the spring crisis. There was, in fact, a considerable net inflow of short-term funds, reflecting liquidation of German short-term indebtedness to the United States, and a movement of balances to this country from Latin America and the Far East. In addition there was a large movement of European resources into the New York security market. Purchases were mostly of American rather than foreign securities.

From the end of the spring crisis until September the greater part of this inward movement of capital was offset by purchases of silver abroad for account of the United States Treasury. There were, however, imports of gold amounting to about $60,000,000 during July and August, half of which was shipped from the Netherlands during the week in which the Dutch Cabinet was overturned. The movement ceased with the passing of the Cabinet crisis.

Aside from the Dutch shipments Europe lost little gold to the United States during the summer months, but losses in reserves suffered by commercial banks in Paris and Amsterdam during the outward movement of gold in the spring were not restored and these centers continued to carry the indebtedness incurred at their central banks at that time. Early in September, when the current gold movement began, reserves were still at the lowest level reached since the international crisis in 1931 and indebtedness was near the spring peak. The cost of this indebtedness has been lowered in France, however, by successive reductions in the rate charged by the Bank of France. From 6 percent on June 20 the bank had lowered its rate by August 9 to 3 percent. The Netherlands Bank, after reducing its rate three times, raised it from 3 to 6 percent during the crisis in July and thereafter reduced it to 5 percent. On September 17, in the face of the renewed gold outflow, the rate was again raised to 6 percent. In view of the substantial volume of indebtedness to the central banks, the course of central bank rates has largely determined the course of open-market rates in Paris and Amsterdam.

The fact that the current movement of gold to the United States led only the Netherlands Bank to raise its discount rate is attributable to several peculiarities in the situation. Pressure on European currencies developed toward the end of August as silver purchases abroad by the United States Treasury diminished in volume. During September there was little further activity of the Treasury in foreign markets and consequently the movement of capital had its full effect upon the movement of gold. The direct shifts in capital between countries, however, did not correspond with the flow of gold. Throughout the month funds continued to be transferred to New York for Far Eastern account; and, although gold began moving in heavy volume from the Netherlands and France, the transfer of funds on Continental account was largely for Switzerland and the smaller European countries. It appears that the Japanese, Swiss, and others who moved balances to this country were for the most part transferring London balances to New York. In addition the British themselves were building up balances and buying securities in New York. As a result the pressure of the capital movement was concentrated on London. The British Fund transferred this pressure to France by selling francs obtained through the release of gold earmarked in Paris. The sale of francs depressed the franc to the gold export point and nearly half the gold received in the United States has consequently come from France. But it has come, not from reserves of the Bank of France which have increased during the movement, but from holdings of the British Fund. In addition substantial amounts of gold reaching the London bullion market from South African mines, Indian hoards, and other private holdings have been transferred direct to the United States. Recently there has been some evidence that the Fund itself has been selling gold in London. It is in the nature of the Fund's operations, however, that they cannot affect either the reserve position of the Bank of England or of the London clearing banks, for its gold transactions are automatically compensated by its purchases or sales of Treasury bills. Hence not only has the Paris money market been unaffected by the gold flow from France to the United States but the London market has also been unaffected by the heavy outward movement of balances and gold together.

The movement of balances from London to New York appears to reflect the disturbing possibilities of the existing situation in Europe and the prominent rôle played in it by England. On the other hand there is little evidence that the movement of gold from the Netherlands in September was attributable to the same cause. Dutch exports of gold began on the eve of the reconvening of Parliament when there was considerable chance that the Catholic Party might withdraw its cooperation with the Government and overthrow the economy program. When the Catholic Party failed to develop a program of its own and voted for most of the Government's measures designed to balance the budget, the gold outflow practically ceased. Dutch shipments of gold to this country during October have been negligible, and the Netherlands Bank has been able to replace through purchases in Paris some of the gold lost in September. On October 17 it reduced its discount rate to 5 percent.

Gold has continued to flow to the United States, however, from England and France. The movement has been moderated somewhat by renewed purchases of silver abroad for account of the United States Treasury.

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BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

February 10, 1937

Mr. Charles S. Hamlin
Special Counsel
Board of Governors of the Federal Reserve System
Washington, D. C.

Dear Mr. Hamlin:

With reference to your letter of February 3, there is attached a memorandum which summarizes data regarding reserve requirements of member banks.

Very truly yours,

E A Goldenweiser

E. A. Goldenweiser
Director of Research and Statistics

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BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date February 8, 1937

To Mr. Goldenweiser

Subject:

From L. M. Piser and Miss Coffey

LMP LC

This memorandum refers to Mr. Hamlin's letter of February 3 regarding reserve requirements before and after the original Federal Reserve Act of 1913.

The reserves required against deposits under the law have varied as follows:

(Percent of deposits)

Class of bank	1874-1914	1914-1917	1917-1936	Aug. 1936 to Feb. 1937	Mar. 1937 to Apr. 1937	May 1937 and after
	Reserve against demand deposits					
Central reserve city banks	25	18	13	19 1/2	22 3/4	26
Reserve city banks	25	15	10	15	17 1/2	20
Country banks	15	12	7	10 1/2	12 1/4	14
	Reserve against time deposits					
Central reserve city banks	--	5	3	4 1/2	5 1/4	6
Reserve city banks	--	5	3	4 1/2	5 1/4	6
Country banks	--	5	3	4 1/2	5 1/4	6

The original Federal Reserve Act reduced total reserve requirements by about one-third. The following table shows reserves held, required reserves, and excess reserves before and immediately after the inauguration of the Federal Reserve System.

NATIONAL BANK RESERVES

Class of bank	October 31, 1914			December 31, 1914		
	Held	Required	Excess	Held	Required	Excess
Central reserve city banks................	409	411	-2	389	306	83
Reserve city banks.....	456	484	-28	424	281	143
Country banks..........	576	538	38	693	371	322
Total.............	1,441	1,433	8	1,506	958	548

The 1917 amendment made a flat reduction of 5 percent for net demand deposits and 2 percent for time deposits at all banks, which on the average offset the effect of the discontinuance of vault cash as part of legal reserves. Banks located in the vicinity of Reserve banks and branches benefited somewhat, however, since they could obtain currency quickly. Banks at a distance found it necessary to keep on hand substantial amounts of vault cash, and consequently held larger reserves than previously or than were apparently required by the law. The following table shows the required reserves for national banks prior to the 1917 amendment and about three months after the amendment went into effect. The decrease in reserve requirements reflects principally the effect of the amendment which removed vault cash from required reserves. Since the banks still needed to hold some vault cash the reserve needs of national banks showed little change between these two dates.

Class of bank	All national banks	Central reserve city banks	Reserve city banks	Country banks
June 20, 1917				
Required reserves.................	1,468	509	443	516
September 11, 1917				
Vault cash........................	492	102	147	243
Required reserves.................	964	377	282	305
Vault cash plus required reserves.	1,456	479	429	548
Percent change in:				
Required reserves.................	-1	-6	-3	+6

The decline in reserve requirements of city banks relative to those of country banks became intensified during the next twelve years. Since vault cash was made a dead asset, neither earning interest nor available as reserves, pressure was placed upon member banks to reduce their vault cash as much as possible. On the average member banks held about one-half as much vault cash as required reserves. By 1929 this proportion had been reduced to less than one-fourth. The most substantial reduction occurred at city banks and the smallest reduction at country banks, as is indicated in the following table:

(In millions of dollars)

Class of bank March 27, 1929	Vault cash	Required reserves under existing law	Total	Required reserves under original Federal Reserve Act.	Percent change
Central reserve city banks...	71	927	998	1,298	-23
Reserve city banks...........	149	762	911	1,166	-22
Country banks................	297	619	916	1,052	-13
All member banks........	517	2,307	2,824	3,516	-20

The 50 percent increase in reserve requirements effective on August 15, 1936, came as a result of a tremendous growth of excess reserves through large imports of gold from abroad. This action of the Board was taken to absorb the idle funds of member banks and to prevent any possible injurious expansion of credit.

The growth in reserves continued in the following months and on February 1 the Board announced a further increase in reserve requirements of 33 1/3 percent. On May 1, when the full increase goes into effect, excess reserves will be reduced to about $500,000,000. The following table shows the required reserves as of January 27, 1937, under the 1917 amendment, under present requirements, and under the requirements effective on March 1 and May 1, 1937.

RESERVE BALANCES
January 27, 1937
(In millions of dollars. Figures partly estimated)

Class of bank	Required: Prior to Aug.15,1936	Required: Present	Required: After an increase of: 16 2/3 percent	Required: After an increase of: 33 1/3 percent	Held
Central reserve city banks...	1,581	2,371	2,766	3,161	3,378
Reserve city banks...........	995	1,492	1,741	1,989	2,147
Country banks...............	504	756	882	1,008	1,248
All member banks........	3,079	4,619	5,389	6,159	6,773