The Papers of Eugene Meyer (mss52019)

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EUGENE MEYER SUBJECT FILE

FEDERAL RESERVE BOARD
F.R. BANK OF NY – CORRESPONDENCE
1932-3

TRANSLATION FINAL COPY

CABLEGRAM FROM PARIS January 15, 1932

TO GOVERNOR HARRISON

24 NEW YORK JANUARY 13 STOP

INFLATION IS THE ORDER OF THE DAY STOP THE FEDERAL RESERVE BANKS AS WELL AS THE LEGISLATIVE ASSEMBLIES SEEM TO HAVE DECIDED TO TAKE THIS ROAD STOP THE DISCOUNT RATE WILL PROBABLY BE LOWERED AT THE NEXT MEETING OF THE BOARD OF DIRECTORS OF THE FEDERAL RESERVE BANK OF NEW YORK STOP THE REDUCTION OF THE BUYING RATE FOR ACCEPTANCES IN THE OPEN MARKET WHICH TOOK PLACE ON TUESDAY IS A PREPARATORY MEASURE TO WHICH THE FEDERAL RESERVE BANK ALWAYS HAS RECOURSE IN SUCH CASES STOP FINANCIAL CIRCLES CONSIDER IT AN INDICATION OF A CHANGE IN MONETARY POLICY AND EXPECT HEAVY PURCHASES OF GOVERNMENT SECURITIES, ACCEPTANCES, AND PERHAPS OF OTHER BILLS FOR THE PURPOSE OF INCREASING THE LIQUIDITY OF THE MARKET AND DEFINITIVELY ALLEVIATING THE GENERAL SITUATION STOP THE EFFORTS TOWARDS CREATING MONETARY EASE ARE ACCOMPANIED BY PROPOSALS TENDING TO BROADEN THE CREDIT BASES AT THE FEDERAL RESERVE BANKS STOP PRESIDENT HOOVER SUBMITTED THEM IN HIS MESSAGE OF JANUARY 4th AND HAS SINCE DEMANDED FROM CONGRESS VARIOUS MEASURES OF THIS NATURE STOP THERE IS REASON TO EXPECT THAT ALL ATTEMPTS TO CURB INFLATION AND HAMPER CREDIT EXPANSION BASED ON LONG TERM PAPER WILL MEET WITH GENERAL OPPOSITION STOP INFLATIONARY IDEAS HAVE SERIOUSLY TAKEN HOLD OF MANY MINDS IN FINANCIAL CIRCLES AND THEIR CONCERN IS MUCH MORE TO CARRY OUT THESE IDEAS AT LEAST IN PART THAN TO LIMIT THEIR DEVELOP-

MENT

STOP WALL STREET IS GENERALLY IN FAVOR OF THE PROPOSED LEGISLATIVE MEASURES AND HAILS INFLATION AS ASSURING AN UPWARD MOVEMENT OF SECURITIES STOP THE MORE CONSERVATIVE FINANCIERS ARE ALARMED BY WHAT APPEARS TO BE THE INAUGURATION OF A NEW ERA OF EXTRAVAGANCE (WASTE) AND PREDICT POSSIBILITIES OF DANGEROUS CONSEQUENCES ENSUING STOP THEY BELIEVE THERE IS NO REASON TO EXPECT THAT BENEFICENT EFFECTS OF AN ERA OF CREDIT EXPANSION WILL LAST LONG AND THEY THINK GOOD RESULTS WOULD RATHER BE OBTAINED BY THE SYSTEMATIC APPLICATION OF OTHER REMEDIES RELATING PARTICULARLY TO FOREIGN TRADE, GOVERNMENT FINANCING AND TAXES STOP THE GREATEST DANGER INHERES IN THE RISK TO WHICH THE FEDERAL RESERVE BANKS ARE EXPOSED IN CONNECTION WITH THE VARIOUS PROPOSALS FOR THE BROADENING OF THEIR DISCOUNT AND LOAN OPERATIONS STOP THE FEDERAL RESERVE BANKS THEMSELVES SOME TIME AGO DECLARED AGAINST ANY CHANGE IN THE DISCOUNT REGULATIONS AND AGAINST ANY BROADENING OF THE CREDIT BASE AS AT PRESENT AUTHORIZED STOP IT LOOKS AT PRESENT AS IF THEY HAD CHANGED THEIR OPINION STOP SOME EVEN INSIST UPON THE NECESSITY OF SOFTENING THE REGULATION IN FORCE STOP IN VIEW OF THESE DEVELOPMENTS CERTAIN OBSERVERS REMARK THAT THE GOLD EXPORT WHICH CEASED SOME TIME AGO MAY EASILY BEGIN AGAIN THE MARKETS WHICH PERMIT THE FREE EXPORT OF GOLD HAVING EVERYWHERE BECOME VERY NARROW

H. PARKER WILLIS

(BANK OF FRANCE)

Foreign Information Division,
January 15, 1932
GL

Discussed verbally
with Ballantyne
at Board Meeting
Thursday
Mar. 23rd/33

THE UNDER SECRETARY OF THE TREASURY
WASHINGTON

March 22, 1933.

TO GOVERNOR MEYER:

Attached is a copy of letter dated March 21st from Governor Harrison in regard to certain foreign exchange transactions, together with a copy of my reply.

I will greatly appreciate it if you will consider this and give us the benefit of your views as soon as practicable.

A A Ballantine

Copy sent to:

Dr. Miller
Mr. James
Mr. Hamlin
Mr. Morrill
Mr. Goldenweiser
Mr. Wyatt
3/25/33

March 22, 1933.

Dear Governor Harrison: FOREIGN EXCHANGE TRANSACTIONS

I have your letter of March 21st in regard to certain transactions in foreign exchange which are being consummated under the Executive Order of the President of March 10, 1933. I should like to consider this question somewhat and shall discuss it with Mr. Kent when he is here tomorrow. I shall then write you further in regard to it.

For the present it seems to me satisfactory to proceed upon the basis which you indicate.

Sincerely yours,

(Signed) A. A. Ballantine

AAB:abm

George L. Harrison, Esq.,
Governor, Federal Reserve Bank,
New York, N. Y.

C O P Y

FEDERAL RESERVE BANK
OF NEW YORK

March 21, 1933.

Dear Mr. Secretary:

I am writing to confirm our telephone conversation this morning with respect to certain transactions in foreign exchange which are being consummated under the Executive Order of the President of March 10, 1933. As you know, this Executive Order provides "No permission to any banking institution to perform any banking functions shall authorize such institution **** to engage in any transaction in foreign exchange except such as may be undertaken for legitimate and normal business requirements, for reasonable traveling and other personal requirements, and for the fulfillment of contracts entered into prior to March 6, 1933."

This bank is required by the Executive Order of March 10, 1933, to report to the Secretary of the Treasury all transactions in foreign exchange in this district which are prohibited. Consequently, we are called upon to interpret the provisions of the Executive Order with regard to foreign exchange transactions and to decide as best we can whether those transactions are in fact in contravention of the Executive Order.

There is one class of foreign exchange transactions about which we wish to advise you. There are, of course, many foreigners who own dollars in this market. As the principal money market in this country it is entirely natural that this should be so, and each day there are current dealings in foreign exchange by foreigners whose dollars have accumulated beyond the amount which they would normally expect to carry, or which are required for other reasons. The purchase of foreign exchange by such foreigners is considered a natural and normal transaction which the banks carry out in the course of the day's work. It does not represent a flight of capital by American holders, but rather represents a repatriation of dollar funds by foreigners wishing, for one reason or another, to bring their dollars home. It is our judgment that it would be inadvisable for the banks to refuse to conduct these transactions so long as they are usual and normal transactions within reasonable limits. To do so would undoubtedly be interpreted abroad as a sign of weakness on our part and it might well result in a severe decline in the quotation of the dollar.

By means of daily reports which we obtain from all dealers in foreign exchange in this district, we keep ourselves currently informed as to the extent of the movements of foreign funds in this market. As long as withdrawals by foreign owners remain within reasonable limits and do not materially weaken the position of the dollar, it is our belief that such transactions may properly be considered "for legitimate and normal business requirements." If, on the other hand, any withdrawals of foreign funds from this market should assume unreasonable and abnormal proportions and would appear to menace the position of the dollar, it would we believe be entirely appropriate to put a stop to such withdrawals as being in contravention of the above-mentioned provisions of the Executive Order.

This letter is merely to advise you of the fact that transactions of this character are being carried on daily by banks and dealers in foreign exchange; that we do not believe it would be advisable to attempt to prohibit them so long as they remain within reasonable limits and do not prejudice the position of the dollar, but that if they should assume such unreasonable proportions as to menace the position of the dollar, we think they might then be prohibited on the ground that they are not "for legitimate and normal business requirements."

Very truly yours,

(Signed) George L. Harrison,
Governor.

Honorable A. A. Ballantine,
Undersecretary of the Treasury,
Treasury Department,
Washington, D. C.

Dictated over the telephone by Miss McCarrick.

Basle
Received May 4, 1932.

PERSONAL FOR HARRISON

(1) THE PRESS REPORTS REGARDING THE GOLDSBOROUGH BILL, THE CONTENTS OF WHICH ARE NOT CLEARLY REPORTED, AND THE VOTE IN THE HOUSE OF REPRESENTATIVES ON IT, HAVE CAUSED A NEW WAVE OF ANXIETY IN EUROPE CONCERNING THE DOLLAR. YESTERDAY AND TODAY WE HAVE RECEIVED PROBABLY FIFTEEN TELEPHONE INQUIRIES FROM ALL OVER THE CONTINENT. CONFIDENTIALLY, ONE SMALLER CENTRAL BANK TODAY WITHDREW ITS DOLLAR BALANCES, SUBSTITUTING INSTEAD FRENCH FRANCS. ANOTHER HAS INSTRUCTED US TO TRANSFER ITS DOLLAR BALANCES INTO GOLD.

(2) MY ONLY PURPOSE IN REPORTING THE FOREGOING, WHICH ~~XXX~~ HAS PROBABLY ALREADY COME TO YOUR ATTENTION FROM OTHER SOURCES, IS TO KEEP YOU ADVISED OF THE SENSITIVE AND NERVOUS DISPOSITION WHICH PREVAILS ON THE CONTINENT IN CONNECTION WITH AMERICAN DEVELOPMENTS.

(signed) MCGARRAGH

Extract from cable of May 4 from Governor Harrison to Mr. McGarragh

I realize that the Goldsborough bill has had a bad psychological effect abroad and while it is not certain what its fate will be in the Senate, nevertheless the reaction against the bill in the press and on the part of the most responsible people have been so widespread and vigorous that we are hopeful that it will be defeated in the Senate. In any event, however, our opinion is that it will certainly be vetoed. As you perhaps know, both Governor Meyer and I have publicly opposed its passage. By many the bill is not considered seriously or else is regarded as wholly innocuous. It was passed by the House, I think, largely as a political gesture on the theory that even if it would do no good, it could do no harm.

But even if the bill should ever become law, which we think most unlikely, you will see from its text that it contains no realizeable threat of currency inflation. Furthermore, its enactment into law would not lead us to make any change in our present policy. The bill reads as follows:

"It is hereby declared to be the policy of the United States that the average purchasing power of the dollar, as ascertained by the Department of Labor in the wholesale commodity market, for the period covering the years 1921 to 1929, inclusive, shall be restored and maintained by the control of the volume of credit and currency. The Federal Reserve Board, the Federal reserve banks, and the Secretary of the Treasury are hereby charged with the duty of making effective this policy."

Burgess?

Plan for Providing Immediate Employment.

(Revised as of June 27th, 1932)

The plans being considered in Congress and by states and cities for relief of unemployed or to provide employment are, first, increased charity on a large scale running into hundreds of millions of dollars, or second, creation of public works which in location, timeliness, and nature and extent of employment required, will not meet the need. The public works will constitute also a continuing liability for maintenance and operation except the "self liquidating" - few in number.

This substitute plan proposes to put to work almost immediately 1,000,000 people and it is believed that a total of 3,000,000 people will be employed who otherwise would not be given employment. As part of the work is seasonal, the objective as to employment is averaged on the base of increase in number of days rather than actual number of employes.

This plan puts the people to work in employment to which they are accustomed and very largely at home, saving the migration of people and the destruction of communities as a result; that is, if people employed are kept in communities already created, values will be maintained, property created there made useful, stores and savings banks kept open; and the incident business and labor activity to all creative industry will be maintained.

Under this plan the very large reservoir of available bank reserves will be employed through normal channels and under existing government and banking agencies including the Reconstruction Finance Corporation, Federal Reserve System, all banks including savings banks, building and loan societies, and the like. These agencies will have the cooperation of the Business and Banking Committees recently set up in each Federal Reserve District with such sub-committees as may be necessary.

Through the use of existing reserves, there will be no call on the government to sell securities to create a loan fund. The only call upon the government will be over a period of time, and when incurred, for actual losses to be paid, these losses to be handled through the Reconstruction Finance Corporation and classified apart from its other operations.

The plan will not put any burden upon the banks but will increase their usefulness. It will be productive in nature and therefore tax bearing instead of tax consuming, which public works program involves.

The plan in its essence is that employers of labor and material, in good standing because of previous record and known character, will agree to employ additional labor and therefore use additional materials, certifying in applying for the loan that such labor and materials would not otherwise be used, that loans will be made with the approval of the Banking and Business Committees referred to and O.K.'d by representatives of the Reconstruction Finance Corporation responsive to such applications. They shall be repaid as fast as the borrower is able to repay on basis of his earnings as indicated by income tax returns. Rate of interest is one per cent above the rediscount rate in that district (but this is open to discussion). Security may or may not be required according to the judgment of the committee that has power to approve. The application may be made to a local bank, which with its recommendation will send it on to the committee or sub-committee, or it may be made direct.

The loans are roughly classified into two groups:

First, those of users of labor and material who have been successful in the past but now find themselves going into liquidation because of inability to secure working capital, the banks being either unable to furnish the money, or desirous in protecting themselves and not taking any chances, of asking for repayment of existing loans through liquidation of inventories and other current assets and the like; this being largely for fear the industry will not be able to supply working capital from other sources.

The second group will be those such as of the railroads and other industries who are deferring all possible expenses in order to avoid charges to operating expenses, and through such avoidance, maintain their black ink situation, showing they have earned fixed charges; and further than that, to keep their cash in position to meet anticipated demands. Many such industries can properly enlarge upon their operations without any question of overproduction being involved.

It is proposed therefore that money advanced shall not involve charges to current operating expenses except with the consent of the borrower, but will be carried in a suspense account as an "anticipated expenditures", and later on, when net earnings make federal income tax payable and these loans likewise become due and are paid, either be charged direct to profit & loss or into the normal operating account as may be decided. With respect to the railroads, counsel and auditor advise me that only the approval of the Interstate Commerce Commission is needed to create such a suspense account with deferred liabilities set up as proposed.

Activities under this plan can cease in any section or with respect to production of any commodity, or as a whole, on action of the Reconstruction Finance Corporation or the President. Of necessity, it decentralizes the power of making loans except large loans; but this will not interfere with current, intensive review of all loans made including classification or cessation of activity temporarily or permanently at any time as may be concluded best.

The plan brings into use the needed experience and ability of business leaders and government finance officers and banks locally gained, on the broad foundation of considering the national and local need for employment and the use of materials; with a quickening of the pulse of business generally it is believed an advance in commodity prices will come since demand depends 75% on employment; and taxation, which is now a tremendous burden, must depend almost altogether on productive employment.

The point of under consumption rather than overproduction has certainly been reached. Shelves are bare; buying in on a hand to mouth basis. Fear and lack of purchasing power have reduced demand tremendously. As to overproduction, the situation canbe safeguarded by limiting the productive activity of any concern to the quantity produced say in the twelve months ending June 30th, 1931. It can be further and perhaps better controlled by stopping activity with respect to the production of any kind of goods if there appears to be an over supply. I firmly believe, however, that the increased payrolls and increase of material we will need, will in almost every direction overcome any problem of presumed overproduction without any marked limitation on loaning power that might be created through this plan. The plan does not go beyond encouraging the activities which would be done in normal times and to a normal extent without this aid. The plan indeed is not intended to go beyond using money and credit to a normal extent as measured say by the twelve months ending June 30th, 1931. If the railroads during the twelve months ending July 1st, spend as much money on maintenance as they did in the twelve months period named, it would illustrate the application of a so-called normal measure to an abnormally depressed situation.

The objections to the plan are plain. The lack of adequate security, the lack of definite time of repayment, errors in judgment which will make for losses, competition in an industry where some people need help and some do not, and use of credit which will in some instances create an unsuccessful activity -- these have been thought of and weighed as against the vast charity distribution we have to make or the great waste of money in public expenditures; and have not been found formidable. There is the advantage that after this plan is tried, it may be changed or done away with and without any undue shock or publicity

Further, it proposes to give help to those who have been successful heretofore; but have not set up a back log of credit because they have not foreseen these abnormal conditions. And to encourage everybody to do the the things they would like to do if they could keep black ink above fixed charges.

It will be noted that the plan provides not for handing out the money, but for contracts for loans; and the borrower must each month make a report in order to secure his money showing that he has lived up to his obligations to provide additional employment of labor and use of materials in accordance with the details set forth in such contract. This is not an impossible condition at all since all large corporations have authority for expenditure requests covering in every detail every unusual expenditure before the work is undertaken; and the cost of the work is then checked up against such detailed requests.

I have attached hereto in detail a suggestion as to how the plan should be made operative. This foreword covers the purpose and the method in a general way.

If I did not feel the railroads could be induced in thirty days to put 100,000 men to work under it that would not otherwise be employed this year, I would not propose it. The test is before acceptance to get them to agree to it.

Memorandum of Plan in Detail

Its objectives are:

(a) Put to work 1,000,000 men in sixty days after machinery established, and as a direct incidence mean the employment of 2,000,000 more,

(b) the work to be productive, of nature to which people are accustomed and therefore fitted, requiring minimum of migration from homes - thus making for least economic waste in personal affairs,

(c) revive industry along normal lines without material waste and save from bankruptcy or absolute disappearance thousands of business activities heretofore successful, and in other instances maintaining a necessary efficiency,

(d) not to interfere with the very vital and necessary efforts of industry to maintain black ink in its operations essential to its credit and indeed to its life; which under existing conditions has necessarily resulted in a narrowing circle of use of both labor and material,

(e) utilizing existing agencies - all banks, building and loan associations Reconstruction Finance Corporation, Federal Reserve System, the newly created Business and Banking Committees in each Federal Reserve District - minimizing additional machinery and expense,

(f) bring into use united experience and ability of business leaders, government finance officers, and bankers to the end that loans may be most wisely made to fit our national need,

(g) enable banks to utilize their great reserves without fear of depositors or loss to either stockholders or depositors, but instead increase the usefulness, security and earnings of banks, saving and loan associations, building and loan associations, and any other financial institutions that may be included,

(h) use the credit of the United States most economically through the Reconstruction Finance Corporation (using as agencies the factors mentioned in (e), to extent necessary with least actual draft in immediate future on such credit in proportion to service that credit will render),

(i) necessitating the establishment of no new government debt to meet the requirement that our people be put back to work; will check inflation later on because of repayments necessary,

(j) the operation to be slowed down, changed or stopped entirely as the need dwindles or disappears, or lack of usefulness is demonstrated,

(k) maintain industry which pays the taxes and upon which the government must depend for existence. In other words, spend the money through tax-payin instead of tax-spending activities. We cannot collect taxes from highways, post offices, bridges or other public enterprises,

(l) would stop many desirable business activities from liquidating their working stocks to meet their debts, such liquidation involving further demoralization of prices as well as putting activities out of business and further reducing employment,

(m) as a final result, entail a very modest loss (comparatively) to the Government from loans made compared with any other avenue of expenditure proposed that will bring back employment; such losses to be realized over a period of time and not immediately.

Use of Government Credit.

(1) Broaden powers of Reconstruction Finance Corporation and enable it to establish additional credit for purpose of restoring employment of capital and labor under conditions that, while giving fair assurance of return of loans with interest, involve risks that banks, insurance companies, saving and loan societies, and building and loan corporations cannot undertake because of their responsibilities to depositors, lenders and share holders; and also loans that normally would be made by such organizations and cannot now be undertaken because of present limitations on their lending powers. Further to induce railroads and other large corporations to undertake maintenance and other work deferred with provision that current operating charges will not be increased thereby.

(2) Agencies to be Employed.

The agencies to be employed are the Federal Reserve System, the banks, building and loan associations, and the Business and Banking Committees recently established, and such other agencies as Reconstruction Finance Corporation may select. (This will save any unnecessary expense in admininistration. Existing loan agencies such as the banks can then carry the loans themselves if they wish, thus utilizing any reserve credits they may have to the extent they choose to do so, with assurance that if need arises, loans will be taken off their hands by the Reconstruction Finance Corporation through Federal Reserve banks when discounted or direct.)

(3) General Rules Governing Loans.

Loans will be finally approved, if not in greater sum than $100,000 to any one borrower, by a committee consisting in each Federal Reserve District ofthe nominees of the Reconstruction Finance Corporation, the Federal Reserve Board, and the Business and Banking Committee recently organized. This committee may either upon the initiative of or by reference thereto be instructed with respect to any particular loan by a joint action of the Governor of the Federal Reserve Board, the principal representatives of the Reconstruction Finance Corporation in that district, and the Business and Banking Committee called as a committee of the whole to consider such loan. The loan committee will also be aided by sub-committees within the three organizations as may be from time to time created by such organizations, separately or collectively. (Separate loan committees may be established in districts geographically large.)

If a loan exceeds $100,000 it must have the approval of the three organizations in meeting called for that purpose. If it exceeds $5,000,000 it must have the approval of the Reconstruction Finance Corporation through its properly authorized officers at Washington, D.C. (These local authorities granted are to secure prompt action necessary, not overburden Washington authorities; the local committee must generally be depended on for informed judgment, anyway.)

The Reconstruction Finance Corporation will have the power to determine the maximum amount of loans to be outstanding at any one time, and will from time to time ratably determine the limit for each Reserve District; and may impose conditions as to loans to any one industry. The borrower must apply for loans within the district in which is located his principal place of business and shall make application only through one channel. One loan does not preclude the borrower from securing subsequent loans. The total loans contracted for, whether or no actually made, shall not at any time exceed five billion dollars. Initially the Reconstruction Fiance Corporation shall apportion a credit among the Federal Reserve Districts in such amounts as it finds necessary.

The borrowers or their predecessors in interest must have been engaged in the business on account of which loan is to be made continuously since January 1, 1930. Loans can be made only for purpose of employment of capital and labor that according to the best judgment of the borrower and as attested to by him would not otherwise have been created. The borrower may be an individual, a cooperative or other corporation or partnership; any institution or individual normally obtaining credit.

Loans shall be made only within a period of two years after the effective date of legislation making such loans available. The Reconstruction Finance Corporation may with the approval of the President suspend the making of loans at any time and for any period. All loans must be repaid within a period of five years except as provided for hereinafter by collections in connection with payment of income taxes. The rate of interest shall be one per cent above the discount rate effective in such Federal Reserve District at the time the loan is made and subject to revision annually in accord with the discount rate in effect as arranged for thirty days prior thereto. Interest payable semi-annually.

The committees having authority to approve loans shall determine what security, ifaany, shall be required but unless otherwise provided when loan is made, any addition in the way of security through such loans shall be maintained free and clear of incumbrance, or other security equal in value given in lieu thereof as security for the loan. No loan shall be made that shall cover expenditures extending over a period of more than two years. No loan shall be made that with his other expenditures will exceed the expenditures of the borrower for like purposes for a corresponding prior period on seasonal or annual basis in the years ended June 30, 1931.

(4) Applications for Loans.

The applicant may apply direct to the loan committee in each Federal Reserve District or to any bank, building and loan association, or other approved financial agency willingto act as agent therefor. He will contract for such loan as will enable him to give additional employment through expenditures for labor and materials. "Materials" will include all supplies and articles of utility essential to his work. He will accompany such application with an Authority for Expenditure Request, such as in use by railroads and other large corporations generally, showing proposed use of the money to be borrowed, its anticipated division between employment of labor and purchase of material, overhead charges, and interest, the estimated time within which it is to be used and all other informative details that will, responsive to the information required in such expenditure request by the Reconstruction Finance Corporation, enable the loan committee to pass promptly upon the loan with a minimum of additional investigation by the agency or sub-committees provided for. If the application be made through an agency such as a bank, then that agency shall in transmitting the request to the loan committee give its views, if any, as to desirability of such loan and the ability and willingness of the borrower to carry out the terms of the contract. The borrower shall in this certificate under oath state that to the best of his belief and judgment the money will provide, insofar as his business is concerned, use of materials and labor that would not otherwise be created; not more than 15% may be used for overhead and interest charges.

If a loan be approved, a certificate shall be issued by the loan committee. Loan shall then be made through an agency of the borrower's choosing or if he has no choice or the agency chosen is not willing to act, then through an agency of the committee's selection. The loan certificate shall be deposited with such agency. Reconstruction Finance Corporation shall provide report blanks on a form on which the borrower may record and attest to the expenditures made in accord with the provisions of the loan contract. Borrower may then call on the agency at the end of any agreed period but not more frequently than once a month with attested statement of expenditures incurred for labor and materials in accord with the terms of the contract, and the agency thereupon will pay to the borrower the amount shown, taking his receipt therefor, upon the loan contract and attaching statement of expenditures thereto as voucher. (It is expected that 90% of loans approved locally will be made through banks as agencies.)

Reconstruction Finance Corporation, if the loan be of any amount requiring its home office approval, will determine the channel through which payment is to be made.

Any bank or other financial corporation so empowered acting as agency for the loan committee may carry loans made for its own account for such period as it may choose and collect interest and principal accordingly; but rendering statement as often as the loan committee shall require of such loans so carried, and status of each. It shall be at liberty at any time to call upon the Reconstruction Finance Corporation through such agency as it may direct (preferably the Federal Reserve Banks) to take over any such loans. Federal Reserve Banks may discount such obligations accordingly. Agencies for the loan committees will be paid for actual expenses incurred under such rules as may be established by the Reconstruction Finance Corporation, and such expenses shall be charged to the borrower.

Loan committee, or any sub-committee, or any agent for either shall at all times have the right to examine the borrower's books or make any other investigation desired with respect to conduct of his affairs that may be related to the use of the money secured through the loan. If agency does not desire to carry the loan, it shall under the rules and through channels provided by the Reconstruction Finance Corporation, be promptly relieved by advances equal to the amount paid to the borrower with interest at loan rate under the certificates of expenditure hereinbefore referred to.

(5) Accounting for Expenditure of Money Secured from Loans.

Inasmuch as the money secured under loans involves expenditures that otherwise would not have been undertaken and which may not immediately return to the borrower any net returns, it may be desirable that all such loans be carried in a suspense account with full detail. The expenditures made thereunder shall not be entered in the normal accounts of the borrower unless otherwise agreed at time loan is contracted for, or later desired, except as and when repayments are made, when with the interest accrued and paid he may dispose thereof with appropriate allocations to capital and profit and loss accounts or direct to operating expenses. Reconstruction Finance Corporation will determine the method of accounting disposition, it being understood, however, that unless the borrower consents, his normal accounting as it otherwise would exist without such loans shall not be disturbed. This is of vital importance and requires careful consideration. Plan must be worked out so as not to interfere with borrower's necessary efforts to maintain black ink in his operations. It is related to provision that loans need not be repaid until borrower makes money as shown by income tax statement. He must have an incentive to borrow and take a chance. The chief cause of dwindling employment is borrower's necessity for maintaining black ink in accounts and cash in banks.

(6) Repayment of Loans.

Loans shall be made for a period not exceeding five years except as repaid through income taxes but may be repaid by the borrower at any time with accrued interest at the end of any calendar month on thirty days' notice. After making allowance for any such payments, the loan will be collected through annual payments equal in amount each year to the income tax paid by the borrower until the whole remaining amount with interest is repaid. Collection will be made at same time and through the same channel as the income tax is collected.

Collection through income tax channels shall be established in 1934 for loans made in 1932; in 1935 for loans made thereafter.

The amount of such collections by the income tax representatives shall be credited to the Reconstruction Finance Corporation; or a receipt showing payment from the holders of loan contract for amount due under this paragraph will be accepted as a credit by the income tax bureau of the Treasury Department.

All loans made hereunder, principal and interest, to extent remaining unpaid shall be due and payable November 1, 1942.

NOTE: The agencies that can give the greatest immediate employment cannot do so unless they have a real incentive. The incentives are:

(1) No call on their cash.
(2) No necessary repayment until as shown by income tax return they can afford it - subject to ten year limitation.
(3) No added "red ink" to current operation through added charges to operating expenses.
(4) Opportunity to repay when money is easy with them or cheap loans available. (It is not probable that money actually will be collected through income tax channels; but the provision will insure collections when borrower has made money.)
(5) The revival of industry which will help everybody.

The question is - will these inducements be sufficient to enable large industrial enterprises to add to their activities? I think so. I will ascertain the attitude of the railroads; am confident they will authorize added employment equivalent to giving jobs to 100,000 men.

As to lesser enterprises or those in more difficult situations who cannot go ahead unless they can borrow money through other channels than normal bank credits, though heretofore successful and enjoying such bank credit. I know personally at least fifty such - perhaps could name a hundred. In some instances the life of a whole community is involved.

The incentive to them is sufficient. They will remain going concerns instead of liquidating, and will give employment and buy material accordingly.

The largest building and loan association on the Pacific Coast has not made a loan in thirteen months. It is pressing collections instead because of constant cash withdrawals. No end of foreclosures are under way. This must not continue or we will have a problem we dislike even to think about. It could, for example, make many loans now to people who wish to build.

Direct relief can be afforded to some extent there; more important is the resumption of employment which will stabilize that situation with respect both to building and loan payments and withdrawals.

The basis of this plan is that the great bank credit reserves shall be made available for loans to increase employment and encourage industry by the assumption of any loss by the government.

There will be loss, but it will be wisely incurred for loans will be intelligently made; and such loss will be small compared with the alternatives.

The dole budget now exceeds $400,000,000 annually if we include community chests and the like. Any national dole legislation will increase this enormously; and pork barrel public work involves such waste, inefficiency as to objectives and continuing liabilities as to be intolerable.

Nor will our income tax returns suffer, even if the incentive be 20%, if plan succeeds; for unless some bold step be successfully undertaken there will be only dried up sources for such taxation.

And again, I would point out such a plan as this with the approval of the President and the Reconstruction Finance Corporation can be dropped, slowed down, modified or for the time being suspended -- almost without notice.

From Geo Harrison

X

July 21-32

BANKING AND INDUSTRIAL COMMITTEE
of the
SECOND FEDERAL RESERVE DISTRICT

July 16, 1932.

Proposals for Putting Credit into Use

1. Public works - Many worthy projects may be found, but measures must be taken to improve budgetary positions of States and municipalities in order that they can borrow. Small reduction in current expenditures or increases in receipts would assure service for large loans.

a. New York City has public works program of 2 billion dollars; authorizations for projects to be undertaken this year have been rescinded to extent of 100 millions and few, if any, authorizations are being made for next year, because of inability to borrow.

b. New York Port Authority projects.

c. Other State and city projects.

2. Private or semi-public construction projects

a. East Side housing devalopment to clear slums and provide cheap houseing. In stage of negotiation with several interested, and sometimes conflicting, parties. Some important questions remain to be solved, but it is possible that if strenuous efforts were made active work of demolition could be started within 60 days.

b. Rehabilitiation scheme - Formation of into groups of large non-competetive companies to supply financing for repairs, etc. of structures now obsolete. Several such groups may be formed to compete with each other. Expected that participants will be able to obtain funds without special action. Question of organization, not of credit.

3. Mortgage funds -

Not only does lack of mortgage money retard new building, but also failure to renew or large payments of principal required on maturing mortgages at this time of reduced incomes necessitates considerable harmful liquidation. Although reduction in mortgage debt is justified on basis of reduced values, postponement of some of this readjustment would materially aid present situation. This will call in some cases for generous measures of relief with some sacrifice of principles of soundness, but in many cases perfectly sound arrangements are possible.

a. Central Savings and Loan Bank of New York - Funds have been promised and this plan may considerably relieve situation in New York State.

b. Aid needed for New Jersey and Connecticut, and probably for other districts, not only to check necessitous failure to renew mortgages, but also to take up those which must be paid.

c. Reconstruction Finance Corporation loans and Home Loan Discount Bank might help to check liquidation.

d. Private corporation in process of formation to finance home construction under new 15-year mortgage plan.

4. Industry and trade -

Numerous complaints received of inadequate credit accommodations from banks. Without detailed credit investigations, difficult to determine whether individual restrictions are justified. Where restrictions are due to bank stringency and not to defective credit standing of borrower, some assistance should be provided.

a. It may be desirable to set up machinery for receiving and investigating individual claims of this nature, and then to find banking accommodation for them. Such procedure may be necessary under Glass amendment to relief bill.

b. Aid may be provided by working with large industrial or local groups that have been hurt by banking difficulties. Toward this end an investigation is now being made of the clothing industry in New York City. Possible measures are (1) formation of new bank; (2) capital contribution by interests in industry to and participation in some existing bank; (3) formation of some sort of finance company by industry.

c. Further investigations of this nature are being made by the National Industrial Conference Board.

d. Trade acceptance plan might provide credits to some concerns to which usual credit channels are now closed.

e. Concerted efforts by large industrial establishments to continue operations and provide employment, accumulating inventories where possible. Many concerns agreeing to follow such a policy might be able to finance themselves; others might need emergency credits of some sort.

f. Financing equipment purchases and repairs and maintenance by railroads and other industries. In some cases economies are possible which would fully justify such expenditures.

5. Organized support to commodity markets.

a. Formation of corporation to buy and hold commodities, selling options for two or three years to consumers. Recent strength in commodities might make such steps unnecessary, or, on other hand, might indicate that such a scheme could now be effective and profitable.

b. Endeavor to induce banks to encourage borrowing for purpose of buying and carrying commodities.

c. Credits to foreign purchasers of commodities, especially in countries where there are exchange restrictions.

6. Security markets.

a. American Securities Corporation is presumably giving organized support to bond market, and speculative interest in bonds seems to be growing.

b. Loans to railroads (and to other corporations) for purchase of their own bonds at depreciated prices. Some plans call for retirement of these bonds; others would permit their sale at higher prices, thus providing corporation with new funds without necessity of floating new issues.

c. Banks might be encouraged to be more generous regarding collateral loans. New loans might now be made on bond collateral. Some banks are now permitting obligors on inadequately secured collateral loans to purchase new collateral instead of making payments on loans.

d. Relaxation of pressure on banks by supervisory authorities. Much has been done in this regard. It has been suggested that shifts in holdings of bonds should be permitted without marking down value of assets.

Burgess

July 22, 1932.

I. COORDINATION OF THE NATIONAL RECONSTRUCTION AND CREDIT PROGRAMS

a. R. F. C. to provide funds to stop liquidation and aid in financing public projects.

b. Federal Reserve to furnish basis for credit expansion.

c. Member banks to extend credit to meet needs of Treasury, R. F. C., and business.

d. Banking and Industrial Committees to discover and promote projects to utilize credit for increasing employment.

II. PROGRAM FOR BANKING AND INDUSTRIAL COMMITTEES

A. National Projects

*1. Securities Markets - American Securities Investment Corp.
2. Commodities.
3. Railroads.
4. Equipment purchases in other industries.
*5. Trade Acceptances.
6. Coordination of district programs.

* Already under way.

B. District or Regional Projects

*1. Public works and public credit.
*2. Home mortgages and cheap housing.
*3. Credit needs of business - by industries.
4. Credit Supply to business - the banks.
5. Spreading work.

* Experts at work on these projects in Second District.

July 23, 1932.

PROGRAM FOR BANKING AND INDUSTRIAL COMMITTEES

It is the primary function of these committees to discover and promote such use of bank credit as will stimulate employment, restore confidence and hasten recovery. They should make every effort, therefore, to bring together sound borrowers and lenders and see to it that no legitimate demand for credit, useful in achieving these ends, is neglected. There will naturally be two principal fields of activity (a) national - (b) district or regional.

A. NATIONAL PROJECTS

1. Security Markets - The American Securities Investment Corporation with an authorized capital of $100,000,000 has already been established for the purchase of sound securities. The question may be raised whether a larger volume of funds should be made available for the operation of this corporation by extending participation to banks or others throughout the country. This question was discussed when the Securities Corporation was first organized, but may well be raised again in developing a national program.

2. Commodities - The advisability of organized efforts in support of basic commodity markets may well be considered. Proposals in this field are discussed in an accompanying memorandum.

3. Railroads - Railroads are an outstanding case where credit might be utilized wisely to increase employment. Railroads could reduce operating costs and improve service largely by replacing obsolete with modern equipment. To accomplish this may

require not only immediate means of financing such improvements but a broader program of bettering the basic financial position of the roads. A corporation organized to lend railroads funds to buy their own bonds and to buy new equipment is worth considering.

4. Equipment Purchases in Other Industries - Methods adopted for financing railroad equipment purchases may be applicable to other industries where similar savings can be effected, thus helping to restore employment in capital goods industries where unemployment is most acute.

5. Trade Acceptances - With the sponsorship of the New York and other committees and with the cooperation of the Federal Reserve Banks, the American Acceptance Council, the National Association of Credit Men and committees appointed by them, a campaign for the wider use of trade acceptances is already under way. This campaign can be further promoted by judicious publicity, both local and national, and the cooperation of Chambers of Commerce, trade associations, and similar bodies.

6. Coordination of District Program - Some informal machinery appears desirable to facilitate an exchange of views between districts, and to avoid duplication or conflict of efforts.

B. DISTRICT OR REGIONAL PROJECTS

1. Public Works and Public Credit - The establishment of a subcommittee, with an expert, to discover and promote means for increasing employment and stimulating activity through public works by cities and states. This project, which is described in the accompanying memorandum, involves dealing with citizen organizations

and promoting budget revision with the objective of improving state and municipal credit in order that these bodies may be in a position to borrow to finance public works in the market, using the facilities of the Reconstruction Finance Corporation only as supplementary to and as an aid to such borrowing.

2. Home Mortgages and Cheap Housing - The establishment of a subcommittee, with an expert, to deal with real estate problems, with the object of stimulating building construction both by arranging a more liberal supply of mortgage money and by discovering and promoting various housing projects as may be economically justified, such as housing projects for the lower East Side of New York. It would be the function of this subcommittee to promote adequate facilities for the renewal of maturing mortgages as a necessary preliminary to the stimulation of new building activity. The rehabilitation of old buildings would offer another field for the activity of this committee.

3. Credit Needs of Business by Industries - Each district committee should set up machinery for exploring the adequacy of the present credit supply for business and agriculture and finding means for supplying credit in cases where it is warranted, but not now available. There may be some question as to how far this work should be done by the banking and industrial committees and how far by departments of the Reserve banks organized under the Glass amendment to the relief bill, but the committee in each district should see to it that the work is done. This appears to involve some survey of business and agricultural credit requirements and the extent to which they are being met, as well as the examination of particular cases which make themselves known. The work may involve leadership

in the organization of credit corporations of one sort of another or other devices for placing business in a position to tap the available supplies of credit. The promotion of the wider use of trade acceptances is one such device.

4. Credit Supply to Business - the Banks. The problem of supplying adequate credit to business involves the added question whether there are difficulties within the banking structure itself which may stand in the way of the banks' supplying adequate funds to business. There may be changes in banking policies, practices, and organization which would enable the banks to meet business needs more fully. Bank policies and practices as to collateral loans, maturity of investments, relations with new customers, etc., may well be examined. It may be well to ascertain the attitude of bank examiners, with a view to seeing whether their policies also are adapted to current developments. In some districts steps may be desirable for restoring banking facilities in communities where adequate facilities no longer exist.

5. "Spreading Work" - A subcommittee, with an expert, to study the possibilities of distributing available employment among the largest number of workers.

6. Other Projects - Various districts will probably present problems that are peculiar to one or more districts and not to others. In agricultural districts, for example, special aid may be needed of a kind different from that required in industrial districts.

July 23, 1932.

PUBLIC WORKS BY CITIES AND STATES

Authoritative estimates now indicate that the total number of unemployed exceeds 10,000,000, an increase of about 3 million over the total for last autumn. This unemployment constitutes the major social and economic problem the country now faces.

There are two possible methods for meeting the problem. One is by providing employment, and the other is by direct relief. Of these two the former is much the more desirable, both socially and economically.

It hardly seems likely that sufficient business recovery - upon which the real solution of the unemployment problem must ultimately depend - will have occurred six months from now to absorb any large proportion of the unemployed in their normal occupations, though every effort should be made in that direction. Meanwhile, the great weight of this problem will fall upon the Federal Government, states, and municipalities. Only a relatively small part of the needed relief can be met with private charity.

At present there is no comprehensive plan of the states and municipalities for dealing with this problem. On the contrary most of them have only been able to secure the money they need for current operations at the price of drastic programs of curtailment. Retrenchment has usually begun at the easiest point for curtailment, which was public works. Thus the total expenditure on public works by states and municipalities now contemplated is considerably less than normal.

The Federal Government program, aside from relatively moderate plans for national public works, is embodied in the relief bill just passed, which provides for loans by the Reconstruction Finance Corporation to cities and states and other public or semipublic agencies primarily to promote activities which will furnish employment. The Federal program thus rests largely upon the city and state programs. While the Federal agency can assist in financing local public works projects, it clearly should do so only in cases where there is a sound budgetary program, which justifies the city or state in increasing its debt. The present financial position of cities and states leaves considerable doubt as to the extent to which they will be in a position to utilize the facilities of the Federal agency.

The principal reason for this situation is that recently city and state financial programs have been determined almost solely from the point of view of the banker and the taxpayer, both of whom are primarily interested in cutting all expenditures rather than in dealing with the unemployment problem. There is clearly need for another approach to the problem by which the budget will be readjusted, not solely with a view to reducing expenses but more broadly with a view to improving the administration, and thereby the credit, of states and cities, placing them in a position to borrow for necessary public works.

The situation in New York City may be taken as an illustration. Last winter when the city needed more funds it was compelled to make a drastic revision of its budget. A first step in this revision was the rescinding of authorizations on projects valued at more than $100,000,000 and offering potential employment to many thousands of workers. No adequate steps, however, have been taken to reduce salaries or to reduce non-essential expenses of government, nor have adequate steps been taken to place the city's commercial enterprises on a self-sustaining basis. If these latter steps were taken New York City could borrow in the market the necessary funds to continue her $100,000,000 program of public works, and so do much to meet the problem of unemployment.

Banking and industrial committees in the several Federal Reserve districts are public bodies which could well undertake the task of organizing public support for budgetary revisions in cities and states which would clear the way for bond issues for necessary public works.

A program of budgetary reform based on these principles would have a much sounder and more effective appeal than a program the sole object of which was to cut expenses and relieve the taxpayer. And, on the other hand, a program of public works could be better justified from the viewpoint of taxpayers, bankers, and municipal officials if accompanied by sound budgetary reform. The social appeal of putting the unemployed to work should constitute a lever powerful enough to force the necessary reforms.

A program of this sort, broadly conceived and energetically carried out throughout the entire country, would not only do much to meet the unemployment problem and promote business recovery, but would as well bring about long-needed reforms in city and state finances and would benefit the bond market both by the improvement in city and state credit and by the issuance of sound new securities.

July 25, 1932.

BANKING AND INDUSTRIAL COMMITTEE
of the
Second Federal Reserve District

ORGANIZED SUPPORT FOR COMMODITY MARKETS

In view of the great influence of commodity prices upon the world business situation, the suggestion has frequently been made that the banking and industrial committees should sponsor some scheme which would stabilize or raise commodity prices. The plans suggested may be grouped under the following headings:

(1) Organization of a corporation to be participated in by consumers of commodities. Basic commodities would be purchased at present prices and options for three years or less sold to stockholders in anticipation of their requirements as consumers.

(2) Organization of one or more private corporations of the investment trust type to speculate in commodities. Such organizations might be similar to the present securities corporation or it might be effected without sponsorship of the banking and industrial committees. It is rumored that some such corporations are already in the process of formation.

(3) Organized efforts to induce banks to be more generous in making loans to consumers or speculators for the purpose of purchasing commodities at present prices and holding them for future use, or for speculative profits.

(4) Some scheme for providing credits to foreigners who may wish to purchase basic commodities in this market. This would apply particularly to purchasers in those countries that are under foreign exchange restrictions.

Reasons advanced in favor of such schemes:

(1), Prices of most basic commodities are at the lowest levels of the century and prices of many are at the lowest levels in history. These prices are well below any reasonably computed costs of production. It is logical to believe that under such conditions prices will rise at some time within the near future. Under these circumstances there are great possibilities for profit to speculators and to consumers anticipating future requirements.

(2) With prices at such low levels and buying in small volume relatively few funds would be needed to provide substantial support. This situation is in contrast to previous efforts at stabilization. Any substantial buying of commodities at this time and firmness of prices would probably lead other purchasers to enter the market in order to anticipate price advances.

(3) Speculative commitments in most commodity markets are much smaller than usual. There is need for a group of buyers to take the position ordinarily held by speculators.

(4) Consumers' stocks are also small and any scheme which would encourage restocking would provide an element of strength to commodity markets.

(5) As in security markets, there are also at times forced sales of commodities by owners unable to hold them further. Under present conditions these forced sales have a demoralizing effect upon the market. Some organized support is needed to broaden the markets and to take care of this type of distress selling.

(6) A rise in commodity prices would immediately bring a change of sentiment in vast world areas devoted to producing raw materials, would increase the buying power in those areas, and thereby give a stimulus to business recovery.

<u>Arguments advanced against such schemes:</u>

(1) Any action which provides only for the purchase and holding of commodities does not change the fundamental factors of production, consumption and

and supplies on hand, which must be influenced before a sustained rise may be expected. The real need is for measures which will increase consumption or reduce production so that the large supplies now available for nearly all commodities can be reduced. If this were accomplished, prices would rise without need for any organized support.

(2) All that most of the suggested schemes, with the possible exception of that providing for foreign purchases, propose to accomplish is simply the shifting of available supplies from one group of holders to another. This may bring about a rise in prices if the supplies are shifted from weak to strong holders who are able to keep them off the market. If this is done, however, by some publicly organized body, knowledge that these stocks are overhanging the market will be an influence of uncertainty similar to that attributed to the Federal Farm Board holdings.

(3) The fact that prices are now below the cost of production has no market significance unless producers actually reduce output or consumption is increased. If production continues in excess of current consumption, there is no fundamental reason to believe that prices can be maintained at higher levels. In many commodities there has as yet been insufficient decline in output to strengthen the technical position of the particular markets concerned. On the other hand, there are probably important shortages in finished goods.

July 25, 1932.

<u>Conclusion:</u> There remain to be settled two questions, one of policy and one of procedure.

The first is primarily a matter of public psychology. If it is felt that public reaction to a program of organized support to commodity markets would be favorable, the next step would be a careful study of the statistical position of individual commodities. Support should then be directed to those commodities whose position justifies the expectation that price improvement could be effected and sustained. In such an advance other commodities would probably share.

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9

(Proposed Letter)

Prepared by Mr. Hamlin July 28-32

Mr. J. H. Case, Chairman,
Federal Reserve Bank of New York,
New York, New York.

Dear Mr. Case:

The Federal Reserve Board has received and noted with interest your letter of July 22, 1932, wherein you advise that, at an executive meeting held on July 21, 1932, your Board of Directors voted, subject to the approval of the Federal Reserve Board, to take certain action which in effect amounts to a reduction in the compensation of all of the employees of the bank, other than officers, in an amount equivalent to 8-1/3% of their present salaries, and a reduction in the compensation of all officers (which it is assumed includes directors) in an amount equivalent to 10% of their present compensation.

The only reason for this action stated in your letter is that the program was "formulated in the light of present employment and salary conditions throughout the country"; and the letter and the inclosed copy of the report of the Committee of the Directors on the Welfare of the Staff contain no discussion of this or any other reason for the action and no reference to the existing situation respecting the earnings and expenses of the Federal Reserve Bank of New York or the possible effect of the proposed action on the welfare, morale or efficiency of the bank's staff.

It appears from previous correspondence and negotiations with the bank regarding proposed increases in the salaries of its officers and employees, and from conversations between Governor

Harrison and members of the Board's staff, that the compensation of the bank's officers and employees has never been at as high a rate as that of persons holding corresponding positions in the larger commercial banks in New York City and is not now as great as the compensation of those employees, even after the reductions which have been made in the compensation of the latter.

It also appears that, since January 1, 1932 the Bank has earned an amount which is not only sufficient to pay all of its expenses, depreciation charges and dividends at the rate of 6% per annum, but also to provide for some addition to its surplus. In this connection, the Board is advised that the bank has book profits resulting from the appreciation of Government securities held by it in an amount exceeding the depreciation charged against its surplus at the end of the calendar year 1931 for the purpose of creating a reserve for depreciation in its bond account, so that the bank's bond account probably will show a net profit and this will result in a further addition to its surplus.

The plan formulated by the Directors for the reduction of the compensation of the bank's officers and employees bears a striking similarity to the provisions for the reduction of the compensation of officers and employees of the United States

Government contained in the Act of June 30, 1932, making appropriations for the Legislative Branch of the Government for the fiscal year ending June 30, 1933; and this has given rise to the question whether the action of the Directors was influenced to some extent by the policy adopted by Congress regarding officers and employees of the Government for the purpose of balancing the Government's budget and, if so, whether the directors were cognizant of the fact that the Legislative Appropriation Act expressly exempts the members of the Federal Reserve Board and its officers and employees, along with all other persons whose compensation is paid from assessments on banks, from the provisions discontinuing leaves of absence with pay and requiring compulsory furloughs without pay, as well as from the provisions regarding reductions in salaries. Also, the question has been raised whether this similarity of action might not add to the erroneous impression that now exists to some extent that Federal reserve banks are government institutions and that their officers and employees are in the general category of officers and employees of the Government. Incidentally, the suggestion has already been made that the Federal reserve banks be required to make detailed reports of their earnings and expenses to the Comptroller General of the United States. In this connection, the Legislative Appropriation Act limits the reduction in compensation of officers and employees of the government definitely to the fiscal year ending June 30, 1933, whereas no definite limitation of time is placed upon the proposed reduction in the compensation of officers and employees of the Federal Reserve Bank of New York.

As to the general question of present employment and salary conditions throughout the country, the Board would appreciate advice as to what consideration was given by the directors of the Federal Reserve Bank of New York to recent developments such as increased factory employment and the upward trend in the general average of wholesale commodity prices which may indicate that the beginning of an improvement in general business conditions is in prospect.

The Board would also like to know whether your directors have given careful consideration to the possible effect of its proposed action on the public and on general business conditions. Such action might encourage other business concerns which have not yet reduced salaries to do so and encourage those which have already reduced salaries to make further reductions. Also, in view of the superior facilities of the Federal reserve banks for gathering and digesting information regarding business and economic conditions, there is a possibility that the public might interpret such action as an indication that the Federal reserve banks are in possession of information which leads them to fear some impending development which would prolong the unfortunate employment conditions from which the country apparently is about to emerge. Such an impression would be increased if other Federal reserve banks should follow the precedent established by the Federal Reserve Bank of New York and reduce the compensation of their officers and employees; and its effect might be equally as potent in discouraging the public and retarding business and economic recovery as the passage of the Goldsborough Bill by the House of Representatives, and in this way any general reduction in the salaries of officers and employees of the Federal reserve banks at this time might prove to be distinctly contrary to the public interest.

You are requested to present this letter to your Board of Directors at its next meeting and to ask that the directors give careful consideration to the questions raised above. If, after careful consideration of these questions, your Directors are still disposed to make a general reduction in the compensation of the bank's officers and employees, you are requested to furnish the Federal Reserve Board for its consideration a full statement of the views of your directors on the subjects discussed above and also the following information:

1. A more detailed and definite statement of the reasons prompting such action

2. The reasons for effecting the proposed reduction in compensation through the furlough system.

3. Whether such proposed action is based upon any operating or financial condition connected with the Federal Reserve Bank of New York as distinguished from general economic conditions.

4. How the present compensation of the officers and employees of the Federal Reserve Bank of New York compares with that now being paid to officers and employees of large commercial banks in the City of New York, after the reductions which have been made in the compensation of the latter.

5. Whether the compensation of the officers and employees of the Federal Reserve Bank of New York was proportionately increased during the time that the large commercial banks in New York were increasing the compensation of their officers and employees and frequently

paying them bonuses at the end of each year.

6. Whether the directors have adopted a new policy which contemplates that increases as well as decreases in the compensation of officers and employees of large commercial banks in New York will hereafter be met by corresponding changes in the compensation of the officers and employees of the Federal Reserve Bank.

7. Whether the proposed reduction in the compensation of officers and employees of the bank is intended to continue indefinitely or is intended to be limited to a definite period.

8. Whether the general economic conditions which in the opinion of your Directors justify a reduction in the compensation of the officers and employees of your bank would also justify a reduction in the dividends paid by your bank, even though the law provides for cumulative dividends.

9. Whether the Federal reserve bank has instituted any special survey of the possibilities of effecting economies in other respects, such as in operating methods, elimination of unnecessary expenses, the reduction or elimination of free services, etc., and, if so, what specific results have been achieved.

Very truly yours,

Chester Morrill,
Secretary.

MISC. 32 60M 12-31

Confidential

(2)

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE September 1, 1932.

TO Mr. J. E. Crane

SUBJECT: Factors governing recent movements of sterling exchange.

FROM E. M. Despres

The purpose of this memorandum is to indicate the factors which have governed the movement of sterling exchange since the middle of June. This date appears to have marked a turning point in the British exchange situation; in order to indicate adequately the character of the change which occurred at that time, a brief summary will first be given of the factors which seem to have been of predominant importance before the middle of June.

Sterling exchange before the middle of June.

Since the suspension of gold payments in September of last year, the Bank of England and the British Treasury had acquired up to the middle of June approximately $800,000,000 in foreign currency assets. Of this amount something more than $550,000,000 had been used to repay emergency credits, totaling $650,000,000, which were obtained by the Bank and the Treasury in New York and Paris just prior to the suspension of gold payments. Of the remainder, it is known that holdings of dollars totaled approximately $160,000,000 and it is believed that holdings of francs are about half of this figure, or the equivalent of approximately $80,000,000.

The factors which enabled the British authorities to acquire foreign funds at the rate of $100,000,000 a month during this period without exerting a seriously depressing influence on sterling exchange will be enumerated in the following paragraphs.

It does not appear to have had its origin in a basic improvement of the British international position. The adverse character of the British balance of payments prior to the suspension of gold payments has been frequently commented upon in the press and elsewhere. Although the decline of

MISC. 3.2 60M 12-31

FEDERAL RESERVE BANK
OF NEW YORK

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sterling exchange has been accompanied by a modest improvement in Great Britain's merchandise balance of trade, this factor has been more than offset by the continued decline in income from overseas investments and from shipping and financial services rendered to foreigners. The strength of the British exchange situation prior to the middle of June appears, therefore, to have been the result of forces of a short-term or speculative character.

Many foreigners owing debts payable in sterling took prompt advantage of the depreciation of the exchange to repay their obligations. Prominent among those participating in this movement were the speculators who had taken a short position in the pound.

The increase in the rupee price of gold, which resulted from the depreciation of the British pound, accelerated the movement of gold from Indian hoards, which was sold, either direct or from the London market, generally to buyers in France, Holland and Switzerland. From the standpoint of its effect on sterling, the principal consequences of this movement were the repayment of certain Indian debts in the London market, and the accumulation of Indian balances there.

A further factor of strength in the British exchange situation resulted from the world feeling of optimism concerning Britain's position following the passing of the critical financial emergency which had existed in the summer of 1931. This sentiment was further sustained by the news of the balancing of the national budget. Supplementing this factor, especially during May and June of this year, were the doubts concerning the position of the United States and its ability to maintain gold payments. While private foreign balances in London were reported to be increasing rapidly, such balances in this country were

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FROM E. M. Despres

reduced to a working minimum. In addition, there were periodic reports of sales of American securities by British investment trusts, and of the transfer to London of investment money derived from sales of American securities by other foreigners. Under these circumstances it is quite clear that in the absence of large purchases of foreign exchange by the British authorities, the pound would have appreciated rapidly.

Sterling exchange since the middle of June.

The change which occurred about the middle of June in the world attitude concerning the stability of the dollar coincided with a marked diminution of the feeling of optimism concerning the British situation. On the one hand, our ability to withstand the final withdrawals on the Bank of France was quite widely interpreted as a sign of the strength of the dollar and the general financial stability of this country. On the other hand, it was increasingly recognized that although the financial crisis in England had terminated with the suspension of gold payments, the general economic crisis in England had not been relieved. Commodity prices, the activity of industry, and employment had shown little or no improvement and the difficulties concerning the national budget appeared not to have been wholly solved.

This change in attitude was reflected both in the movement of short-term funds and in the international movement of securities. Short-term funds figures collected by this Bank show a decline of $50,000,000 in "due from" England from June 8 to August 24. Reports from London indicate that this outward movement of American funds was only a part of a rather general withdrawal

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of foreign short money from the London market. A portion of the funds which were withdrawn from London were transferred to this country in the form of short-term balances, but an examination of our own short-term fund statement would appear to indicate that these funds were transferred more largely to our security markets. Moreover, reports have been current, appearing both in the British and in our own financial press, of substantial British purchases of American securities. Although no quantitative data are available concerning foreign buying of American securities, the existence of such a movement may be inferred from the fact that the recent inward gold movement cannot be wholly accounted for in terms of the other items in this country's balance of payments.

In addition to the psychological factors indicated above, the movement of sterling exchange has been influenced in recent weeks by a seasonal increase in imports of raw materials by Great Britain. Although this factor does not become of great importance until the autumn months, bills financing the movement of cotton and other raw materials to England have already been noted in the foreign exchange market.

In consequence of these adverse factors, the British authorities appear to have considered it desirable to render financial support to sterling exchange. Despite a reduction of $70,000,000 in British official funds in this market since the middle of June, and presumably some drawing down of official balances in Paris, the pound has declined from $3.66 1/4 on June 15 to $3.47 on August 31.

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Note concerning Movement of Short Term Funds

Short term funds figures collected by this bank give some indication of the importance of the movement of short money between this country and England as a factor in the recent weakness of sterling.

In millions of dollars

	1932		
	April 6*	June 8	August 31
"Due to" England			
Official (Treasury and Bank of England)**	113	110	49
Private	58	43	51
Total	171	153	100
"Due from" England	88	116	67
Excess "due to" England	83	37	33

* First reporting date following final repayment of American private credit to British Treasury.

** Does not include dollar deposit of Bank of England with B. I. S. It is known that Bank of England's dollar holdings through B. I. S. increased during the period from April 6 to June 8, and that they were subsequently reduced.