FEDERAL RESERVE BOARD

STATEMENT FOR THE PRESS.

For release in the morning
papers Tuesday, April 15th, 1919.

The Federal Reserve Bulletin for April was sent to the printer today. Its publication has been deferred for some days in order to furnish at the earliest possible moment the official statement of the Secretary of the Treasury, concerning the fifth, or Victory Liberty Loan. A large part of the Review of the Month, which, as usual, is the leading feature of the issue, deals with the conditions of the loan and the banking situation, as affected by it. After quoting at length the statement of the Secretary of the Treasury, in which the terms of the new offering are stated, the Board discusses some of its salient features as follows:

"So clearly are the terms and conditions of the new issue set forth in the Treasury statement" says the Review "that comment would seem to be called for with respect only to one or two points in connection with the announcement. Of these the most important is probably the character of the new offering as an issue of 'notes' rather than of 'bonds'. The new notes, under the terms which have been fixed by the Secretary of the Treasury, are to run for not over four years. Practically, therefore, the difference between the old and the new issues is that while the Government must redeem or refund the notes after a given period it might or might not, at its option, refund the older issues. There is evidently no warrant whatever for the view that the notes are essentially a different kind of investment or are to be regarded in some special or peculiar way as contrasted with the bonds. They are like the latter Government obligations, while the period of their life is entirely sufficient to warrant the ordinary investor in putting his funds into them. Indeed, as is well known, before the war one of the most important conservative investments in the money market of the United States was offered by a series of short-term notes issued by railroads and public-service corporations. These had become a favorite investment with discriminating buyers, their maturity being from one to five years, the preferred life as a rule not exceeding two or three years. When the investor purchases a Government note with a maturity of four years he has the assurance that the obligation thus purchased will possess greater stability of value than could possibly be given by any bond whose maturity is long or which is subject to the possibility of redemption after a specified period, but which has no definite or positive claim for such redemption upon the maker or issuer of such bonds. Far from its being true, therefore, that the new 'notes' are not well adapted to private subscription, they are eminently so adapted, while the conditions under which they are to be issued should bring them much closer to the requirements of the individual buyer than has been true of any of the preceding Liberty Loans."

The Review then describes the financial situation which has called forth the new offering of notes, saying that this is so well known that only a very general description of the circumstances attendant upon the placing of the issue need be furnished.

It is noted that

"the Treasury has, from the beginning of December last to the end of the month of March issued in certificates of indebtedness intended to anticipate the proceeds of this flotation approximately $4,700,000,000, after deducting exchanges and redemptions. These obligations run five months from their date of issue. At the present time the expenditures of the Treasury are running at the rate of about $1,300,000,000 per month, a figure decidedly less than the rate of expenditure in January and about the same as that which was established during February. The exact outlay for March has been $1,379,811,785. Estimated expenditures up to the end of this fiscal year will bring the outlay for the fiscal year as a whole to about $18,000,000,000 or $19,000,000,000 of which sum there had been expended up to the end of March $15,164,224,227. Congress has in the meantime adopted legislation designed to afford new sources of revenue from taxation, the first installment of which was turned into the Treasury on March 15. This legislation, however, will not suffice to meet the requirements of the Department, as the figures already furnished amply show."

The Board also comments upon the fact that the new loan will all be used, as pointed out by the Secretary of the Treasury in his statement, for the retirement of outstanding certificates of indebtedness, which have been issued in anticipation of the sale of the notes. On this point the Review continues as follows:

"The policy of issuing short-term certificates of indebtedness was resorted to by the Treasury Department early in the war at a time when the needs of the Government were exceptionally urgent and unexpected in character. They have served their purpose well as a means of supplying the Treasury without delay with the funds of which it stood in need. In so doing, however, the certificate policy has necessarily placed upon the banks the necessity of bearing a continuing burden of war securities.

This burden was, of course, at a minimum immediately after the conclusion of a Liberty loan, inasmuch as at that time at least a considerable part of the new bonds had been sold to the public and the certificates to that extent 'funded'. In so far, of course, as a Liberty loan did not result in inducing the public actually to take over and pay for the new bonds, the banks instead of carrying the short-term certificates of the Government now carried the paper at whatever date maturing, which had been made by their clients for the purpose of enabling themselves to subscribe for bonds. Inasmuch as the process of borrowing by the Government against certificates has almost invariably been begun within a very short time after the completion of a Liberty Loan, there has been steadily in the hands of the banks a varying quantity of certificates which has increased as the date of flotation of each Liberty Loan drew nearer, thereafter to be technically reduced by the public through the process of borrowing at the banks for the purpose of absorbing the bonds. The necessity of general public subscription as an indispensable element in the process of financing thus becomes apparent."

Attention is then called to the necessity of securing a wide popular distribution of the new notes, as against the condition in which they might be left in the hands of the banks, and the statement of the Secretary of the Treasury, issued on March 12th, wherein broad subscription to the notes was urged, is quoted. The Review then comments upon the necessity of taking up the notes as generally as possible, saying:

" "It should be understood that under the plan of financing which has been pursued by the Government since the entry of the United States into the war, the direct source from which public funds are drawn is the commercial banks of the country. Precisely this same situation exists in the case of the fifth loan, and precisely the same obligation rests upon the community to participate in the purchase and absorption of the bonds needed for the funding of the certificates. During the continuance of the war there was, of course, the impetus growing out of the belief that subscriptions made in this way were necessary for the purpose of aiding in the immediate maintenance of the armies in the field. The Government still has strong military forces in Europe engaged in the important and necessary work of completing our operations there. The obligations which have been met since the opening of the year and are still to be liquidated are those which remain subsequent to the conclusion of the war, and which represent the obligations or indebtedness incurred for the conduct of the struggle. Essentially, however, the reason why the public should subscribe for and take up the securities offered in one of these great periodical loans is that of self-interest. If the obligations already taken by the banks are not liquidated, the community at large will suffer from a continued inflation of banking credit and from the high prices that are consequent upon this condition of affairs. Only one remedy for the situation now existing can be applied - that, namely, of subscribing freely for the Government obligations when offered and of paying for them out of the proceeds of saving, either already accumulated/or to be accumulated from time to time. Indeed, the urgency for adherence to this policy is greater now than it was during the war, inasmuch as at that time there was strict oversight and control on the part of the Government over production, distribution, and, in a measure, consumption, while at present that oversight has naturally and properly been greatly relaxed,or, in many branches of business entirely abolished. The responsibility of saving and conserving resources thus remains with those who are the recipients of current incomes, either from investments or from salaries and wages, in perhaps a higher degree than was previously true.

"Neglect on the part of the public fully to appreciate and fully to perform its duty in taking up and paying for the forthcoming Victory note issue", says the Review, "would have a very prejudicial effect upon the banking position by aggravating the state of credit expansion which already exists." It is pointed out that, under the Income Tax law approximately $1,001,000,000 have already been received as a first installment. "This", says the review, "is currently accepted as equivalent to about one-quarter of the total return to be expected, but is probably in excess of that figure. While probably the large majority of individuals and corporations will prefer to take advantage of the installment method of payment, there are not a few who are following the custom of former years of paying in lump sum. Such payments tend relatively to reduce the payments to be received at subsequent installment periods. There is no means of estimating with accuracy the total return on the basis of the installment of March 15, unless it be assumed that this installment is roughly equal to one-quarter of the total, in which case the gross income from the income, corporation and excess profits taxes will amount to not more than $4,000,000,000."

The moneys received on March 15 served to liquidate issues of certificates of indebtedness which were falling due on that date and consequently simply to transfer a specified amount of bank credit from one group in the community to another through the medium, first, of tax payments to the Government, and then liquidating payments made to meet its outstanding certificates. Inas much as practically $800,000,000 of the March 15 receipts were thus absorbed in settling maturing claims, the first tax payment leaves the Treasury in about the same position as before, so far as current payments are concerned, and it must therefore dispose of the same problem as heretofore in connection with its program of borrowing and expenditure."

After thus discussing the situation as to the prospective fifth loan, the Review takes up the question of railroad financing and points out that this matter is now definitely shifted to the War Finance Corporation under the plan already announced, whereby that organization cooperated with the Director General of Railways. The War Finance Corporation bond offering of April 2nd is described and the Review then turns to the general commercial paper situation, saying that

"Renewed purchases of commercial paper by banks are reported, while not a few institutions are stated to be considering the best methods to be followed in the use of their fluid funds when short-term Treasury certificates of indebtedness shall be withdrawn from the market. The volume of funds available for private industrial enterprises has seemed to be reasonably satisfactory, although rates have been kept at a tolerably high level as a result of the conservatism of bankers who desire to avoid the development of any cramped position which might result from the demands of the Government during the progress of the fifth loan. While the Government is still supporting the export trade in no inconsiderable degree, it is noteworthy that a substantial percentage of the new financing now in progress is intended for the purpose of facilitating the movement of goods to foreign countries. These credits are taking the form in many instances of acceptances, while in others they are simply ordinary advances designed to sustain business which is being developed for export account."

The recent Belgian industrial credit is cited as an example of current peace borrowing for the rehabilitation of European countries, whose productivity has been impaired by the war. On the question of foreign exchange, the Review, after referring to the suspension of governmental control, or "pegging", says that

"These changes in the situation of exchange mark the beginning of a new period in international finance. The withdrawal of Government support in important branches of exchange is equivalent to a statement that henceforth the movement of commodities for private account between the United States and other countries must be financed on some basis other than that of Government guaranty. In normal times the decline of exchange occurs in countries adversely affected by an unfavorable balance of trade.

The effect of such an adverse balance is to depress the rate of exchange and thus to raise the price of imported commodities in the country which is suffering from a fall of exchange and a tendency is thus automatically set up to restrict further excessive buying by importers. Great Britain has already found it necessary to adopt strong measures to prevent further importations of commodities and the withdrawal of support for sterling will tend to make these restrictions still further effective. The same situation will probably exist in an even more marked degree with respect to importations from the United States into Italy. All these conditions must necessarily exert an important effect upon our export trade. Indeed, the extent to which we can now export to foreign countries which have lately been belligerent will depend upon their ability to finance their own needs, or to obtain adequate assistance in such financing from American banks and bankers. Undoubtedly such assistance will be forthcoming in considerable measure, but it can hardly be expected that so tremendous a flow of goods out of the United States will be maintained as has been true for a long time past, giving us during the years 1916-1918 a favorable merchandise balance of about $9,000,000,000. So far as it is thus maintained, the result will be accomplished only through action on the part of Americans looking to the purpose of financing foreign buyers in their purchases. This, in other words, means that the United States, in order to continue as a great exporter, must also continue as a great investor in foreign countries, and that to the extent she is able to do so her selling power will be correspondingly developed and sustained. It must soon become a question, therefore, through what agency and methods the American investor can best be reached in entering the field of foreign investment.

"A special situation had developed early in March in connection with French exchange. The most striking feature of these occurrences was a marked decline in the international value of the franc - French francs being quoted on March 18th at 5.80 per dollar, since when the quotation has fallen below 6 francs. The decline of the French franc has been variously attributed to developments in connection with French Government financing, to a deliberate relaxation of the control or "pegging" of French exchange by the Government of France, and to other factors. The truth of the situation is that our payments to France, both through Government loans and through disbursements for the Army on the spot, have greatly fallen off. New credits opened by the United States Treasury to the French Government since the armistice and up to the end of March amount to only $285,000,000, while the withdrawal of fully half of our troops and their transfer back to the United States has correspondingly decreased the amount expended for soldiers' pay and expenses. France has not and will not for some time to come be in a position to export effectively, and the destruction of much of her northern industrial region, and the disorganization of other producing sections, as well as the delay caused by the necessity of converting her war plants to peace uses will necessarily retard still further the development of her power to ship salable goods. France must therefore contemplate for a considerable time to come a situation in which she must either purchase less abroad or must expect in the absence of artificial control an unfavorable state of the exchanges. The removal of the restrictions by France upon the movement of gold would involve the shipment out of the country of a considerable volume of the metal for the purpose of equalizing exchanges, and this makes it less probable that there will be such a restoration of the free movement of gold in the immediate future.

"From the standpoint of the United States, the continuance of large exports of grain and foodstuffs which have kept the record of January, February, and the early part of March fully up to that of any corresponding period in the past, means that foreign countries will be under the continued necessity of finding satisfactory means of settling with the United States for goods which they are not in position to offset by means of corresponding exports of the United States. This suggests that the exchange problem may become more pressing. Both it and the question of gold embargoes will need to be considered at an early date. Meantime, it is worth while to note that the Treasury still has limited powers of extending financial accommodation to foreign countries."

The usual review of business and financial conditions during March is included in the Bulletin and, in addition, there is published a series of statements from the Federal Reserve Banks with reference to the liquidation of war paper now in their hands. Among the other features contained in the issue are a description of current indexes of business conditions, and a translation of the law extending the charter of the Bank of France, together with a review of its war operations.