

Paris, February 24.

After consideration of your telegram under reference, the Ministry of Colonies and the Ministry of Foreign Affairs have come to the conclusion that instead of attempting further to agree upon the proposed definition, it is preferable to abandon the proposal to abrogate the present bonding system. In other words, they now propose to leave the Decree of April 9, 1935, regarding the bonding system for the exportation of alcohol from St. Pierre in full force and effect.

In addition, the Ministry of Foreign Affairs states that if there should be any continuance of smuggling they will be prepared to reexamine the situation. Furthermore, that the Administration of St. Pierre will receive special instructions from the Ministry of Colonies to supervise the importation of alcohol into the Islands so that, if necessary, measures may be taken to prevent the building up of new stocks.

We have attempted, with the support of the Ministry of Foreign Affairs, to obtain in addition to the retention of the Decree of April 9, 1935, a new Decree prohibiting the importation of foreign alcohol into the Islands. We have pointed out that the Administrative Council has submitted for the approval of the Ministry of Colonies a resolution of September 29, 1936, prohibiting the importation of foreign alcohol, and that all that would be necessary would be for the Ministry of Colonies to give its consent. The Ministry of Colonies, however, states that at the same time as the foregoing resolution was submitted, it was understood by the Administrative Council and the Administrator of St. Pierre that the present bonding system would be suppressed. The Ministry of Colonies, therefore, takes the position that if they are now to maintain in effect the present bonding system they can not, in view of the foregoing understanding, approve the resolution which would prohibit the importation of foreign alcohol. The Ministry of Colonies, furthermore, states that so long as the Decree of April 9, 1935, governing exportations is in effect, there is no necessity for prohibiting the importation of foreign alcohols.

Inasmuch as the present bonding system is to remain in force, the French Government, instead of issuing a decree prohibiting the manufacture of alcohol in the Islands, renews to us through the Foreign Office its assurances that the manufacture of alcohol in the Islands, in fact, will not be permitted.

I should appreciate a reply at your earliest convenience.

BULLITT.

Feb 25, 1937

236

from Masell

OBJECTIVES

Improvements in Bureau Administration.

1. More prompt and more equitable determination of income tax liability.

a. A simpler income tax return.

b. Better revenue agents' reports.

(1) More adequate information for the Bureau

(2) Fewer unfounded or poorly determined deficiencies

c. Adequate settlement machinery gradually moved to the field: give the taxpayer a real opportunity to settle his liability promptly in his own locality, with a Treasury man who knows his business.

Both (a) and (b) to be accomplished by detailing good conferees and attorneys to the local internal revenue agents' offices.

d. A supervisory flying squadron,

(1) To check revenue agents' examinations and settlements

(2) To instruct agents and help preserve consistency in practise

e. Large cases in general to be dealt with in Washington.

(1) Drive to settle back years which are holding up settlements of current years

f. Collectors coordinated with revenue agents; and their staffs under Civil Service

2. Improvements in disposition of litigated cases.

a. Clarification of relations between the General Counsel's office and Technical Staff.

(1) General Counsel to be charged with full responsibility of settling or defending cases brought to the Board of Tax Appeals

(2) Technical Staff to aid on technical side: engineering, audit, valuation.

- 2 -

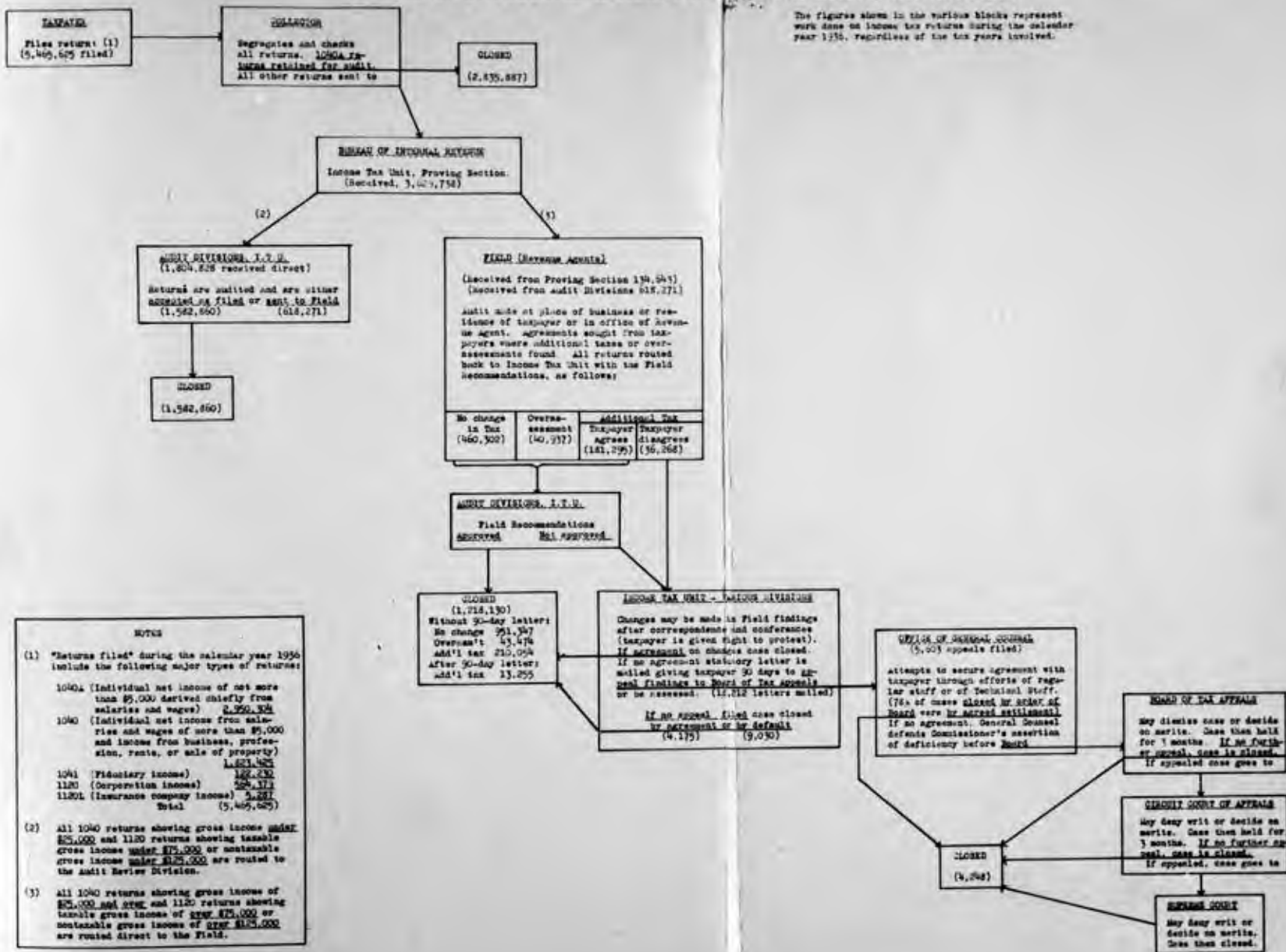
- b. Settlements and refunds to be disposed of more promptly.
- c. Revision of procedure of Board of Tax Appeals.
 - (1) Can we get the Chairman to designate a Committee to study the matter and report.
- d. Revision of statutory provisions which now permit three tax suits (Board of Tax Appeals, Federal District Court, Court of Claims) where one is enough.
 - (1) Eliminate suits against Collector:
 - (a) The procedure is complicated and no useful purpose is served.
 - (2) Eliminate suits for refunds in Federal District Courts and Court of Claims.
 - (a) If this is done, the Board of Tax Appeals will be given jurisdiction instead. Hence the Board must be induced to perfect its procedure first.

Tax Legislation.

- 1. Can we eliminate the tax-exemption of future issues of State and Federal bonds.
 - (a) So long as tax-exemption exists, Federal taxation based on ability to pay is largely stymied.
- 2. Board to formulate plans for State-Federal coordination.
 - a. Coordination should be within reach if the Treasury makes up its own mind as to what the major sources of Federal revenues are to be.
- 3. Economic and legal staff to prepare ideal Federal revenue system this Summer and Fall.
 - a. Greater proportion of revenues to come from taxes levied on basis of ability to pay. (e.g. income, estate and gift taxes)
 - b. Further equalization of taxing system as between corporations and individuals.
 - c. Careful re-examination of excise taxes, leading to elimination of many.
 - d. Codification of more permanent provisions of revenue laws: revised statutes, prior acts, current laws.
- 4. Revision of court procedure provisions, in direction of greater simplicity.

OUTLINE OF PROCEDURE LEADING TO CLOSING OF INCOME TAX RETURNS

The figures shown in the various blocks represent work done on income tax returns during the calendar year 1950, regardless of the tax years involved.



MEMORANDUM

February 25, 1937.

To: Secretary Morgenthau
From: Dr. Burgess

Government bonds were higher today, having moved up sharply in the forenoon on the Secretary's announcement. There was a brief period of fairly active trading with good demand for long bonds and "rights"; trading was rather quiet thereafter. Quotations advanced further in the final hour, Treasury bonds closing generally 3/32 to 7/32, and Guaranteed bonds 3/32 to 6/32 above yesterday. The 2 3/4s of 1951-54, 2 7/8s of 1955-60 and 2 3/4s of 1956-59 reached new highs. In the note market the April 1937 3s rose 4/32; the rest of the list was generally 1/32 higher on the day, with two issues 2/32 better.

Second grade domestic bonds made gains of up to 1 point during the forenoon in a fairly active market. Some selling appeared toward the close, rails and industrials finishing small fractions above yesterday and utilities mixed. In the high grade market the low coupon refunding issues finished slightly better on the day; others were approximately unchanged.

Foreigns were quiet and steady in the forenoon but rather irregular thereafter in moderately active trading. The decline in Polish bonds continued, with losses of from 4 to 6 points. Canadian bonds were slightly lower; Italians mixed; Germans were slightly higher.

No purchases for Treasury today.

McL

Gray.

London.

Dated February 25, 1937.

Received 12.20 p.m.

Secretary of State,
Washington.

96, February 25, 1 p.m.

FOR TREASURY FROM BUTTERWORTH.

London press this morning carries agency report under Washington date line to the effect that other schemes for stopping the influx of foreign capital into the United States have been dropped as unworkable in favor of a gentleman's agreement with Britain; "under this agreement it is suggested the British Government would discourage British investors from purchasing American securities. It is pointed out that such action would help to keep British credit fluid for armament needs".

FINANCIAL NEWS quotes Professor Sprague as expressing doubt whether foreign funds will be withdrawn from the United States and attaches significance to the fact that Sprague has just sailed for England on the QUEEN MARY.

At the annual meeting of the National Mutual Life Assurance Company of which he is chairman Maynard Keynes referred to his remarks of last year (my 67, February 20, 6 p.m.) and expressed the opinion that the proposed rearmament borrowing was well within this country's capacity

-2- 96, Feb. 25, 1 p.m. London.

capacity, citing that the sinking funds of public boards and local authorities, collections of building societies, post office deposits and industrial reserves alone should amount to 400,000,000 pounds each year. He concluded therefore it was thin the power of the Treasury to get its money without producing conditions of inflation and added that the question of the rate of interest "is entirely a matter of management and how the task is handled". He also emphasized that it is a popular error to suppose that the rate of interest today is exceptionally low; "there was not a single five year period between 1837 and 1914 when the average yield on long term gilt edge securities was as high as it is today".

In this general connection O R Hobson comments that short of a drastic credit ratio system it is impossible to postpone capital expenditure other than by the natural means of allowing the rate of interest for new borrowing to rise "and short of deliberate inflation of credit I for one believe that the rate of interest will rise; even with inflation it will ultimately rise for inflation means higher commodity prices and higher commodity prices mean that both the Government and other borrowers must borrow more than they would otherwise have had to do".

Keynes also made the following comparison of the techniques of the British and American Treasuries: "In our own case by far the greater part of the debt (apart from Treasury bills) has no fixed date of repayment within the next

-2- 96, Feb. 25, 1 p.m. London.

next twenty five years-in round numbers five billion pounds is long dated in this sense and only about one billion pounds of intermediate date. Moreover, nearly half of the securities of intermediate date stand above par and are therefore inconvenient holdings to many investors for tax or other reasons. In the United States on the other hand practically the whole of the debt is repayable within 25 years; indeed there is nothing beyond 30 years. And within the next 25 years there are notes or bonds falling due for repayment in almost every year. Thus every taste is suited, a rate of interest rising slowly as the date of maturity becomes later; for example the taxfree rates are about one quarter per cent for one year, one per cent for two years, one and one quarter per cent for four years, one and three quarters per cent for six years, two per cent for ten years, rising to two and one half per cent for fifteen years. These rates do not greatly differ from the net redemption yields on British Government securities for comparable periods; but the arrangement of the maturities allows the American Treasury to borrow at a materially lower average rate. It is to be remembered that many holders of gilt edged securities are primarily interested in security of capital: and whilst there are others who are attracted by security of income over a long period it is unlikely that these latter are five times as numerous as the former. It is therefore expensive for

the

96 from London

-3-

the Treasury to keep the longest dated market in relative overdraw supply. They should profit from the anxieties of the public and save interest by supplying them with the potential liquidity which they demand."

ARTHURTON

RB

GRAY

Paris

Dated February 25, 1937

Rec'd 3:05 p. m.

Secretary of State

Washington.

273, February 25, 3 p. m.

FROM COCHRAN.

Paris exchange market today featured by strong demand for dollars. Market operators say New York began selling sterling last night and British control gave up important amount of dollars in unsuccessful effort to hold rate at 4.89. Dealing in sterling at Bank of France today not very important, forward franc weak as end of month approaches. Rentes down. Internationals better. Swedish crown exceptionally strong following talk of revaluation upwards.

Bank of France statement as of March 19 showed no change in gold stock or in advances to state.

European financial press carries report of Professor Sprague's departure for Europe. Some writers suggest connection between his visit and American study of capital influx problem. Press impression today is that United States will not place a penalty tax on foreign capital but will

-2-#273, February 25, 3 p. m. from
Paris

but will resort to "gentlemen's agreements" with other governments to place a check on funds moving toward New York. French press prints extracts from Runciman's remarks upon his American visit with particular attention to possibility of Anglo-American trade pact (END SECTION ONE)

BULLITT

HPD

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PARAPHRASE OF TELEGRAM RECEIVED

NO.: 273, Section Two
FROM: American Embassy, Paris
DATE: February 25, 1937, 3 p.m.

This morning I talked with President Trip of the Netherlands Bank at Amsterdam over the telephone. I informed him that when I was in the United States, whence I had returned a few days ago, we had tried to take steps which would facilitate the smooth working of the reciprocal gold arrangement between club members. To this Trip replied that his relations were entirely agreeable and that his gold dealings through the New York Federal Reserve Bank were moving smoothly. It was his opinion that we should not worry too much about developing the mechanics of the operations involved until after the immediate problem is settled of the finances of one of the three original club members. The French outlook was giving Trip considerable concern. The French, he told me most confidentially, had tried to secure a credit of five billion francs on the Dutch market but had been refused. President Trip does not believe that France would really be helped if domestic confidence is established. Unless there is some political change in the country, he does not think that such confidence is likely to be established. He perceives no early likelihood that a real change will occur.

EA:EB

BULLITT

Regraded Unclassified

TREASURY-FEDERAL RESERVE-S.E.C. GROUP February 25, 1937
ON RESTRICTION OF FOREIGN CAPITAL INFLOW 3:15 P.M.

Present: Mr. Magill
 Mr. Oliphant
 Mr. Goldenweiser
 Mr. Bryan
 Mr. Gardner
 Mr. Eccles
 Mr. Upham
 Mr. Haas
 Mr. Gaston
 Mr. Francis Green (S.E.C.)

H.M.Jr: Well, let's start. The bond market went up four or five thirty-seconds on the announcement.

Eccles: Of no new money?

H.M.Jr: Yes. Had a strong bond market.

Eccles: Yes.

H.M.Jr: And right at the end it just gave a "phwit." I mean the last five or ten minutes.

Eccles: Well, it's working all right, just like planned so far.

H.M.Jr: So far. All right, gentlemen, let's go.

Magill: Well, I believe the order of business as agreed upon at either the last session or some intervening one, was that we prepare memoranda with respect to the suggestion which the President made that we might be able to modify these withholding rates in the case of persons who had held the investments for a long time, providing a lower withholding rate for foreigners who had held the investments for some years, as distinguished from a higher rate for people who had just bought in.

I think I might as well read this memorandum. Or shall I speak it? It doesn't make any particular difference. Whichever goes easier.

Oliphant: That's the memorandum that you (H.M.Jr) wanted in such shape that it could be shown around.

- 2 -

H.M.Jr: I haven't seen this, so....

Magill: Well, we went into it. I think I'll speak it.

H.M.Jr: Have you got a copy for Eccles?

Magill: Do they have a copy over there?

Gardner: We'd like another one over here.

Eccles: Oh, this is the withholding.

Magill: The withholding tax at a graduated rate, depending upon the length of time held.

Oliphant: If you got a copy of that yesterday, I completely rewrote that, so don't...

H.M.Jr: This starts off "At a conference on February 17...."

Magill: Well, who took the one I just gave to somebody? I don't have but this other copy.

H.M.Jr: Well, why don't you read that? Then we'll make sure we're reading the same thing.

Magill: "At a conference on February 17, there was submitted to you a plan for increasing the withholding rate of tax on income received by non-resident aliens and foreign corporations. You suggested further study of this plan with a view to avoiding an increase in the rate of tax on income from long-term investments. This further study has been made and the conclusion is that the plan, modified in this fashion, cannot be made administratively feasible because, unlike a transfer tax, it would require the determination of the identity of the foreigner, the nature of his interest and the length of time he had held the securities in question. These facts could not be satisfactorily determined for the following reasons:

"1. In the case of stock, the records of its ownership in the United States are not sufficient because a considerable amount of stock has been held abroad for many years in the name of banks, brokers, or other fiduciaries, with no reliable records in this country and available to the Treasury indicating the actual owners of such stock.

- 3 -

"The great mass of bonds are unregistered bearer bonds and debtor corporations in this country have no records of the actual owner of such bonds other than the name disclosed on ownership certificates presented at the time of interest payments. These certificates cannot be wholly relied upon because transfers of ownership can take place without any corresponding change in these certificates of ownership.

"2. The Bureau could not depend upon statements of identity, interest and period of ownership made by foreign investors because of the danger of their being self-serving. The Bureau would be unable to verify such statements by actual inspection of the foreign investor's records, and the Government would have no control over the person of a foreign investor enabling it to set up penalties effective to prevent the making of false statements.

"3. In the absence of reliable records as pointed out above, it would not be feasible to adopt arbitrary rules as to ownership, such as a rule treating record ownership as actual ownership, or arbitrary rules as to period of ownership. Such arbitrary rules would have to be made so narrow in the process of preventing evasion that they would give relief to only a small class of long-term investors.

"In the case of stock, to accept record ownership as actual ownership would place a premium on stock held abroad for a period of years especially by banks or brokers because foreign investors would seek to acquire stock so held without transferring record ownership since dividends on such stock would escape the higher tax rates. It would create in many cases two prices for the same security. Again, a rule that ownership remains unchanged until record ownership is changed would permit and encourage dealing in stocks held by banks and brokers.

"4. Finally, any plan imposing two widely divergent rates of tax operating simultaneously would create serious administrative difficulties if the lower rate of tax was to be confined in actual operation to the class of foreign investors entitled thereto.

"(a) The attempt to apply different rates of

- 4 -

withholding at the source would impose upon withholding agents the additional burdensome obligation of ascertaining the facts necessary to determine in the case of each interest or dividend payment the proper rate of withholding.

"(b) To require withholding at the maximum rates in all cases and adjustment thereafter by the Commissioner would entail a severe administrative burden upon the Bureau of Internal Revenue and require additional appropriations to make such refunds. In such cases also the Bureau would be confronted with the problem of securing adequate proof of the foreigner's identity, his actual interest in the securities in question and the length of time he had held them.

"Note: The great mass of the foregoing difficulties would not be present in the case of a transfer tax because, in the latter case, it would be necessary to determine merely one fact, viz., that a particular transaction involved a foreigner. His identity would not have to be determined, the character of his interest would not have to be ascertained, and the length of time he had held his securities would not have to be considered."

In other words, the substance of it, I take it, is that the record ownership in case of securities would not in reality be any indication of the real ownership of such securities, and it would be difficult or impossible for us to ascertain what the real ownership is.

- H.M.Jr: There's a lot of people missing here today. (On phone) Ask Mr. Taylor if he's coming into my office, and Mr. Haas whether he's coming into my office. And Mr. Gaston.
- Magill: Now, do you want to discuss that or shall we go on with the alternative proposal?
- H.M.Jr: Well, how about Mr. Eccles? Do you want to discuss this?
- Eccles: Well, I don't want to discuss this. It seems to me that - I have been opposed to this approach to it anyway. I mean it seemed to me that the withholding tax in itself was...

- 5 -

H.M.Jr: Excuse me a minute, Marriner. (On phone) Hello? Yes. O.K. - - Taylor's over at Farm Credit.

Eccles: I'm glad that this is the finding, the conclusion.

H.M.Jr: Well, I mean do you want to - if it's agreeable to you that I send it, I'll send it over my own signature - but I mean....

Eccles: Yes, you can say as far as I'm concerned that...

H.M.Jr: You don't - I mean you don't want to take time to analyze it. You're willing to take our crowd's word for it?

Eccles: Yes, certainly. If you had some other conclusions, we might want to, but the conclusions are what I had hoped and expected.

H.M.Jr: Inasmuch as it says no, you won't object?

Eccles: That's right.

H.M.Jr: All right.

(Haas and Gaston come in)

(On phone) Hello? Is Mr. Francis Green on the wire? May I speak to him? (Has short conversation, unrecorded, with Green)

Said Mr. Landis spoke to him yesterday, but inasmuch as he didn't talk to him again he didn't know he was supposed to come.

Magill: Takes two to make an appointment, I guess.

Eccles: Well, is Landis away?

H.M.Jr: Landis went up to Harvard and is going to be gone for the rest of the week. But I simply felt that - he felt that if he had this thing... I wanted to clear this particular thing, so - I mean the President sort of put this hurdle up and I thought the thing to do was to say whether we could handle it or not, and the answer was...

Eccles:no.

- 6 -

H.M.Jr: The answer was no. I'll just send it over, unless you (Oliphant) want to have another chance to look at it.

Oliphant: I want to retype that first page.

H.M.Jr: I'll have it done.

(Reporter leaves on errand for Secretary; returns)

Oliphant:foreigner is involved, who he is, what his interest is, and either how long he's held it in case you want to give relief to the long term investor, or what he gave for it in case you've got a capital gains tax. It really boils down to the administrative feasibility or lack of administrative feasibility; boils down to the fact that you have to ascertain three or four facts in order to apply those two or three taxes.

H.M.Jr: Well, except in the capital gains - the market value as of the effective date of the tax.

Oliphant: You've got to ascertain who he is, got to get his identity, ascertain what his interest is, whether he owns it or somebody else owns it, ascertain what he gave for it.

Eccles: Not that necessarily.

Oliphant: To get his capital gain, what he gave for it and what he sold it for.

Eccles: Not if it is a flat capital gains. A flat capital gain applies not at the basis of his cost. If he acquired it at a certain date, I don't think you can go back on a capital gains tax and tax the profit that has accrued up to a given date; your capital gains would apply to profit that accrues after the effective date of the law, which of course would be a deterrent so far as new capital coming over. In other words, the prospect of capital coming in in the future, buying securities, getting appreciation, would be of course hit for all earnings that they make. But earnings made up to this time - in other words, profits on stocks - of course I don't think that you could figure on a capital gains tax that

- 7 -

would be retroactive so far as...

Oliphant: Oh yes, you could. It's common. In fact we've always done that, haven't we? That is...

Eccles: I think it could be, but not practically.

H.M.Jr: Now wait a minute. This suggestion to the President is just going to wipe that to one side.

Oliphant: Yes, it isn't feasible. That's the reason I tried to summarize.

H.M.Jr: What are you going to take up next? We're not going too fast now, are we?

Eccles: I merely raised this question when Herman mentioned the capital gains tax, an objection to it, and I questioned that particular objection, was all. I don't think we should discuss the capital gains tax.

H.M.Jr: Let's dispose of this.

Eccles: Any way that you people want to dispose of this is agreeable to us as long as the answer is no.

H.M.Jr: Well, I'm just going to send it over. "My dear Mr. President: For your information I am sending you herewith the enclosed memorandum." I'll just sign it and don't have to bother you with it.

Eccles: That's fine.

H.M.Jr: I mean so as to keep the thing moving, that's all. Where do we go from here? That's what I want to know.

Magill: Well, we have prepared one other document. Now, you see, we've got two alternatives at this point. If the President agrees with us that it is not feasible to make this adjustment which he talked about, then he might either think that the proposed increase in the withholding rates ought not to be done and that we ought to suggest some other alternative to that, or else that the proposed increase in withholding rates that we suggested is all right; in other words, go

- 8 -

through with the plan as we originally suggested it to him, or he might say, "Is there any alternative?"

H.M.Jr: Well, have we an alternative?

Magill: And that's the next thing.

H.M.Jr: Next thing. O.K.

(Francis Green comes in)

Green: So sorry to be late, sir.

H.M.Jr: That's all right. Why don't you take a minute, Magill, and tell Mr. Green about this memorandum. Have you got an extra copy for him?

Magill: Have you any more carbons of it, Herman? I'll give you my own copy if...

H.M.Jr: Or - what I suggest, Mr. Green, is - if you don't mind, if you'll stay afterward and talk with Mr. Magill, he'll explain about that, because I'm a little pressed for time today. That memorandum is going to the President in answer to a question....

Green: Yes, sir.

H.M.Jr: ...which he raised.

Green: Yes.

H.M.Jr: He made the suggestion could you do this thing in a certain way, and the people felt you couldn't. And that's the formal document which I'm signing.

Green: Yes, sir.

H.M.Jr: But I'd like you to keep up with it, and if you'd stop afterwards and drop into Mr. Magill's office, you can read it in there, and if there's anything you don't understand he'll explain, and we won't have lost any time.

Magill: Well then, the other memorandum which we have prepared is on this assumption: assuming that the President doesn't like our original proposal on

- 9 -

the basis which we have submitted in the previous memorandum; namely, that this adjustment in the case of long term investors cannot be made; and that he wants an alternative. This is the alternative. Shall I read this too?

H.M.Jr: Please.

Magill: "If the proposal for an increase in the rates of withholding tax, as originally submitted, is not acceptable, then the following substitute or supplementary plan is submitted for consideration:

"Impose a tax on the transfer of corporate securities by or to a foreigner at a rate based upon a percentage of the sales or purchase price. To achieve flexibility, a minimum and maximum rate should be prescribed and the power given to the President, on the basis of designated finding and proclamation, to fix the effective rate. The operation of the tax will be substantially the same as in the case of the present transfer tax on corporate securities.

"The broker, agent, or other person acting for the buying or selling foreigner in the execution of the purchase or sale would be responsible for the collection of the tax. Within the United States on the established exchanges, where the bulk of the transactions will take place, the tax would be effective. Transactions occurring outside of the exchanges, however, would present difficult problems (particularly in the case of bearer certificates or certificates in 'street' names). The tax would tend to increase the number of the latter transactions but this would perhaps not endanger the objective since most of the business is and would remain in the hands of responsible brokers who would not seek the avenue of evasion with its prospective penalties.

"The operation of the tax within the United States will tend to create a premium on American securities available for sale abroad without the payment of the tax. The tendency would be for citizens and resident aliens to attempt to obtain the benefits of this advantageous market by sending their securities to Canada or abroad. The following steps may be taken to check any such flow of securities from the United States to Canada and Europe:

- 10 -

"(1) The American citizen or resident alien who sells or purchases securities of a domestic corporation outside of the United States would be made liable for the tax with heavy penalties for nonpayment. There would be a presumption in such case that the other party to the transaction was a nonresident alien. Discovery of the transaction would not be certain but the ever present possibility of detection, through examinations in connection with the income tax and returns of information filed by third persons, would be a powerful deterrent.

"(2) Penalties would be provided for any domestic corporation (or its registrar) which recorded on its books the transfer of any security from or into the name of an alien, unless the tax thereon had been fully paid.

"In the administration of the tax, the principal fact to be determined will be whether the purchaser or seller is a foreigner. The identity of the particular foreigner will not be in question. Hence, the operation of the tax will not be impeded by the prohibition placed upon originating foreign brokers who are usually subject to laws or usages prohibiting disclosure of the identity of the principal."

Well, briefly, on that, as you know, we now have a tax on transfers of securities based - well, it is four cents a share in case of par value stock, and also in the case of no par unless the stock sells for more than \$20 a share, in which case it is five cents a share.

Now, our thought, I think, as we have it in mind in a rough way, for purposes of having something specific to think of, would be that it would be desirable anyhow to revise our present stock transfer taxes, which, as you can see from my statement, have nothing whatever to do with the value of the security. Your rate of tax is very low in case the security is sold, and it may be very high in some cases where the price of the security is low.

Hence, it would seem advisable - I may add to that that the tax is one which will be cut in two on July first anyway unless action is taken, so that

- 11 -

we'll have to take some action with respect to the domestic tax in any event.

Eccles: That expires July first, does it?

Magill: It doesn't expire; it's cut in two on July first.

Eccles: I see.

Magill: So we had tentatively in mind that what we might do is this: change that tax so that it is imposed at some fraction of one percent upon the value of the security transferred, fixing that fraction to yield us the same amount of money which we now get, which would be about one tenth of one percent of the value of the security transferred. It is now based on par or no par and a very rough affair.

Eccles: Yes.

Magill: And then we thought we would impose the same rate of tax upon transfers to or from aliens, but provide that the President may increase it or decrease it in the event of certain findings of fact.

Eccles: In other words, the deterrent, of course, to foreign buying of American securities would be the extent of the discretionary power....

Magill: Right.

Eccles: ...vested in the President.

Magill: Right.

Eccles: Now, if that is high enough, it should be - it seems to me that it ought to be high enough to make it a really effective instrument.

Magill: Well, the information Mr. Haas has given me - he can check me on this - is, as I understand it, that if the rate of tax were about one percent of the purchase price, speculative transactions would just about be stopped. Isn't that right?

Haas: No, three percent, so you'd want it three percent.

Magill: I thought you thought one would do it.

- Haas: No, three percent, on the basis of the turnover now of the securities in this market held by foreigners - about a three percent would take such a slice of their capital away that it just about makes it prohibitive for a speculator. But one percent wouldn't do it, because you have one percent or about that in England.
- Magill: Yes.
- Oliphant: Say you bought a hundred dollar security - I mean in-and-out trading - speculating in and out, and paid three dollars tax. If he turns over ten times, he's lost thirty percent.
- Haas: He'd pay a three dollar tax, pay his commission, and pay his carrying charges.
- Oliphant: Three dollars would be plenty.
- Haas: Yes, I think so. We were talking about one in another connection.
- Eccles: Would three percent be enough? I can understand that with the trader, with a man that is buying and selling as traders do. But as I understand it, a large portion, the great bulk of our securities that are being purchased today are not purchased by traders so much as by institutions and individual investors with an idea that they'll hold them for an indefinite period. They too are after the speculative profit that is likely to accrue to them as a result of an appreciation in these values, but not in the same way as is the American trader who is in and out all the time; he's constantly scalping the market; of course, this would exclude that type of a foreign operator.
- Oliphant: I want to point out that for a foreigner to go in and get this profit that you say he is after, he'd have to pay two commissions, six dollars in tax.
- Haas: That's both ways.
- Eccles: Oh, both ways. Well, I see.
- Oliphant: And he'd have to pay his carrying charges.

- 13 -

- Eccles: Well then, a six dollar tax - that is, six dollars on the hundred - and the commissions, would certainly - if he disposed of them within a year's period, even in many instances a two years' period, he would receive no earning whatever on his investment while he held it. And of course that would be a deterrent because I think foreigners buying stocks now don't want to be in the position where they may have to hold them for three or four or five years in order to get any return on them. They want to be in a position, certainly, within a year or two years, to dispose of them. Wouldn't you think that that certainly is in the back of their mind?
- Magill: Yes.
- We looked up the transfer tax, just as a matter of background, in the neighboring countries, or the countries which are doing the principal investing in this country. In England I believe it works out to be about one percent of the value throughout; they've got a graduated scale, but that's about what it amounts to. In Canada the rate of tax is about the same as our present tax. There is both a provincial tax and a Dominion tax, and they seem to range between about one fifth of one percent on some transactions down to about one fifteenth of one percent, or thereabouts, on others - on the larger transactions. France is a little better than half of one percent. Switzerland is a tenth of one percent.
- Oliphant: What's Germany?
- Magill: Germany is - I think it's - let's see, Germany is fifteen hundredths of one percent; that's about one sixth or one seventh of one percent.
- Eccles: We haven't had an opportunity to study this....
- H.M.Jr: Neither have I.
- Eccles: ...this thing, so that our...
- H.M.Jr: Neither have I. And this technical background, of course, is available to both organizations. I mean they just finished this at noon today.
- Eccles: There's one or two, it seems to me,.....

- H.M.Jr: Well look, why don't - if you feel that way, Marriner, why don't we do this? Why don't both the Federal Reserve and S.E.C. let the technical staffs get together and pick this up, what we've got, and study this thing, and then meet early next week.
- Eccles: That would suit me all right.
- H.M.Jr: Either organization can give birth to something. And what we touch upon in this thing certainly interests S.E.C. - what we're talking about.
- Eccles: Mr. Landis...
- H.M.Jr: He'll be back Monday morning.
- Eccles: He favors something of this sort.
- H.M.Jr: I don't know.
- Eccles: I mean what I understood here - he had in the discussions here referred to a transfer tax as a desirable and effective means of getting at speculative activity on the part of foreigners.
- H.M.Jr: I just want to say this, that during the week I have changed to this extent, and I'd like you to know about it. I don't know how you feel, but I don't want to march up to the Hill with a recommendation which we know beforehand isn't going to reach the people we are after, namely, the fellow who does use "hot" money, see? - and just have them say, "Well, all you're doing is reaching the permanent investors. The suggestion you make is all right as a revenue measure or measure of equity, but if you are really after hot money, what you are suggesting is a joke."
- Eccles: Well, I'm glad you've come to that conclusion.
- H.M.Jr: I mean over - we haven't met in a week, since we had that long talk with Mr. Hull, and I'd just like you to know that my thinking has changed to that extent. I mean after all, I.... You (Green) tell that to Mr. Landis.
- Green: Yes.

- H.M.Jr: My position has shifted to that extent. If I'm going to march up on the Hill there, I think we ought to have something which we think has at least got a 75 percent chance of being effective.
- Eccles: Well, I'm glad that you've come to that conclusion. I feel exactly the same way about it. I was willing to go along with the withholding tax as a - I wasn't hopeful of it being effective in doing the thing that it seems is going to be necessary to do. And in proposing it at all, it was expected of course that we would say that this is merely the first step and that it was looked upon as a minor step, and so on. Now, I believe that it is much better strategy to defer action - to defer any definite proposal until we feel reasonably satisfied that what we do propose will have at least a fifty-fifty or a seventy-five - or I'd say it ought to have at least a fifty-fifty chance of doing what we are trying to accomplish. I'd just as soon do nothing until we have reached that.
- H.M.Jr: Well then, we - I mean I'd go further. I'd like to feel, if I am making a recommendation to Congress and asking them to hurry it through, that in my own mind and in the minds of my associates in the Treasury at least, we can say, "Well, we've got a 75 percent chance of being right."
- Up to now - after a week and all that... And then just simply have - as an effect of that, have any other country that has any decent-sized stock exchange slap on the same thing; and find that we haven't kept the funds from - they're rolling in just the same. I'd feel awful sick over it.
- Eccles: Yes.
- H.M.Jr: What?
- Eccles: I think it would make us look pretty foolish.
- Golden.: Mr. Secretary, may I stick out my neck by telling my reaction to the transfer tax at this time?
- H.M.Jr: Oh, you've got such a nice neck, do it.
- Golden.: Well, my feeling about it is that it would not

- 16 -

materially diminish the net inflow of capital and it would drive business from American brokers to foreign brokers. It would be a tax whose incidence would be on the business of American business men engaged in the legitimate business of stock brokerage.

Eccles: If that is legitimate.

Golden.: Well, it is so far recognized as legitimate.

H.M.Jr: You forgot who was sitting here.

Green: We suppose it is legitimate, see.

Eccles: I said...

H.M.Jr: Well, they're supposed to have legitimized it.

Eccles: That's right.

Golden.: Well, it's going to make them lose business to foreign brokers and it isn't going to stop the flow of money. That is my impression of that tax.

H.M.Jr: Well now, I want to know - due to press of business, my people weren't able to give me this until now, so I'd like the week-end to digest this thing. And I think this is particularly something that S.E.C. wants to find out about, because if they put their name to it and the result is what Dr. Goldenweiser says, that you are driving business to Canada, London, and Amsterdam, you've got to be prepared to defend it.

Green: That is, of course, the danger about which the S.E.C. is worried; that is, we may transfer the real market in American issues to foreign markets if we precluded trading in those securities in American markets.

H.M.Jr: But you'll notice someone said this suggestion of increasing the transfer tax was - they thought was Mr. Landis's suggestion.

Green: Well, I should think that it could be coupled with other restrictions designed to prevent the export either of American securities or of European shares for American securities, which they would have to have in order to run any substantial market in London

- 17 -

or in continental cities.

- Eccles: I made that statement, but I didn't mean this particular proposal. But isn't that true, Bryan, that Mr. Landis had a program of this sort?
- Bryan: Well, I think Mr. Landis has spoken of transfer tax a couple of times. I don't believe in any of their direct memoranda they have outlined a specific proposal.
- H.M.Jr: Well, Marriner, personally I don't think that we can go any farther than we have today. I think certainly I couldn't, and I'm sure Mr. Landis and S.E.C. generally want a chance to look at this new idea. And then sometime early next week let's get together again.
- Eccles: Fine.
- Magill: Now, if I may say something, stick my neck out, which is not beautiful. I wish you two groups would go at it in the way that we have been trying to go at it here in the last week; that is, not merely to shoot holes in this proposal, which is not too difficult to do, but to suggest other ways and means which may occur to you to implement this one. Or, for instance, your (Green) suggestion about the export of American securities. Maybe we'll have to amend your Act; maybe it isn't simply a taxing proposition.
- H.M.Jr: And the other thing which I... Are you through?
- Magill: Substantially, yes.
- H.M.Jr: If you're not...
- Magill: Go ahead, that's all right.
- H.M.Jr: The other thing I want to say, in strictest confidence, so that you know what we are doing - we are making a very, very confidential study here of what we should do in case a major war should break out in Europe in regard to this eight billion dollars here, and when we get along a little further on that we'd like to show it to you. But that has nothing to do.... I mean going the whole way; I mean the idea of possibly

- 18 -

having a custodian for securities owned by aliens. But we've just started. But Senator Nye said he couldn't handle it, that it was too much for him; and he was down here. And the President asked us to do it. But I just want to tell you in strictest confidence that we are doing it, and after we get somewhere we'd like to show it to you, to both of the organizations. But we're going the whole way. I mean in case a major war should break out, what would we do? But I'd like - I'm saying that in strictest of confidence.

Eccles: I think that we'd better defer action until we can think this thing all the way through in connection with its ramifications. We've got to at least see far enough in advance so that we know what our objectives are. Otherwise, we - it seems to me we may make proposals that make us look ridiculous.

H.M.Jr: True.

Eccles: And I think the thing you're doing is certainly an essential part of this whole problem, and to be forearmed, it seems to me, is the height of wisdom.

H.M.Jr: I think so.

Eccles: So far as our approach to this is concerned, Magill, we realize that it is one thing to make constructive suggestions and it is another thing to come along and simply criticize and have nothing to offer. Now, I talked to our people about this several times and have said to them, "Assume that we alone, see, had this responsibility. Now let's approach it from that standpoint. What would we do? We're not trying to find reasons why there isn't anything we can do about it - why you can't do this or why you can't do that. There is a problem that must be met. Let's start from that premise. Now, what are the various ways that we think we can meet it?" And that is the way we are approaching it, and certainly it is the way we want to.

H.M.Jr: That's right.

Magill: For instance, just consider this. Suppose we went through with our first proposal, with this modification: that we simply provided that the President

- 19 -

might increase the withholding rates or later decrease them, based upon the application of certain standards, but left withholding rates at the present just exactly where they now are. Secondly, suppose that we modified the transfer tax along the lines we have indicated here this afternoon; same tax on aliens that is on our domestic people but at a percentage of the value, with the power in the President to make changes.

And then, if you wanted to consider a third thing in the chain, suppose we took out the exemption of capital gains in the case of non-resident aliens and put in a flat ten percent tax.

Eccles: Yes.

Magill: Didn't do any more.

Eccles: Capital gains, you mean?

Magill: Yes.

Gardner: With the necessary machinery?

Magill: No machinery.

Gardner: Machinery to...

Magill: Well - and the fourth possibility, machinery.

Gardner: Which machinery would serve in the case of a war program.

Eccles: Yes, that's another thing.

Oliphant: What I'd like to do is simplify my own work by getting clear on the terms of reference. What is the problem we are studying? I understood we started out to study the problem of putting a damper on the type of funds - speculative funds - going into our stocks here that is creating this movement of gold. Now, are we also now undertaking the problem of regulating the trading in American securities abroad, which doesn't affect the flow of funds? If we are going to do both, it is a different problem.

- 20 -

- Green: The latter problem is one which has been advanced by the technical people of the S.E.C. And if American money is going abroad to be used for speculation on foreign exchanges, it seems to me that is a little different matter than the one that Mr. Eccles has just...
- Oliphant: Well, American money going abroad to be used on speculative exchanges abroad - that is the opposite of foreign money coming here for speculation. I just want to be sure of our objective.
- H.M.Jr: Well, Mr. Green gets it and I think that...
- Oliphant: ...that we are trying to do two jobs at once.
- Green: I wonder if any other agencies are interested, at least to some extent, in American money going abroad to be used for speculative purposes over there.
- H.M.Jr: I can say that after all that is your responsibility.
- Green: Yes
- H.M.Jr: I know what Mr. Oliphant is getting at, and I don't think it is really part of this study.
- Oliphant: Not our responsibility.
- H.M.Jr: It's your (Green) responsibility.
- Green: I agree with you, but I can't say so officially.
- H.M.Jr: Well, I'll say so for you.
- Green: Right.
- Gardner: Your proposition for a three percent transfer tax means that it costs three percent to get your American security over to the London exchange. After you've got it there, then there are no more transfer taxes to pay. If you had to keep trading on the American market this three percent tax would mount up and up and up. Now, the Englishman who looks for a hundred percent or fifty percent profit -

- 21 -

what will stop him in a three percent transfer tax if he can do his trading in the London market and not pay the tax?

- Oliphant: Well, his trading in the London market cannot cause gold to flow here. And that problem of initiating additional foreign speculation abroad is dealt with in the latter part of the memorandum.
- H.M.Jr: Well, may I just - if you want to stop it, we know how to stop it, because we stopped silver trading in America; but we just sent it to Montreal and England, that's all. I mean the fellow who was willing - if he made a profit he knew he had to pay a fifty percent tax. He bought his silver in London or Montreal. But we closed the silver exchange in New York just by that law.
- Golden.: Mr. Secretary, may I just say one other word. Mr. Oliphant's formulation of the problem is that the problem was to prevent the speculative flow of funds to America. Now, I think that word "speculative" tones down what I always thought was the problem. The problem was the capital movement to this country and a large gold inflow, speculative or otherwise. If you want to discriminate as between different flows, we'd probably be prepared to be harder on the speculative than on the non-speculative; but the problem as it was presented and the problem that we have tried to tackle is the problem of the inflow of foreign capital at the rate of a billion or more a year to this country, which is bringing in a lot of gold and complicating our economic - our whole financial structure and raising the issue of what's going to happen when it is...
- H.M.Jr: That isn't what your boss said when he walked out of the White House.
- Golden.: Isn't it?
- H.M.Jr: No, he didn't say that?
- Eccles: That is, the problem that we've got to deal with - now, the speculative aspect takes this place, that the greater part of capital today is coming over here and going into the speculative market; that

- 22 -

part of foreign capital that lies idle in the banks as a deposit does no harm because it is just lying there, and that part of foreign capital that comes - except to the extent that the gold is bought and there is an interest charge against the purchase; but the deposit is not getting into our circulation, it isn't responsible for inflationary prices, and it does very little harm. And the capital that comes over here that buys our commodities is of course giving employment. The capital that buys our securities - that is, our bonds, our mortgages - is of a particularly small proportion. So that you get at the real evil at the moment, at least, when you get at the speculative aspect.

Now, I don't say that if you deal with the speculative inducement of foreign capital - when you take that away, that capital may not continue to come over here in an amount which, although greatly reduced, is still an amount much more than we desire, and at some later date we may have to do something about that.

Oliphant: Well, trying to find out what the problem is,...

H.M.Jr: That's what Oliphant's trying and I...

Oliphant:I would accept Dr. Goldenweiser's statement of the problem, and then say that for practical purposes, in my own mind, that problem had been deleted by our discussion at the White House which, for practical purposes, eliminated this long term investment stuff. So that I understand that the problem for us now...

Eccles: That is, present long term investments that are here.

Oliphant: The problem now is to deal with this type of quick in-and-out stuff in such a fashion that we will change this picture whereby now Europe is buying on balance every day, so that when we get through operating on it Europe will be either not buying on balance or may be selling on balance, and that when we have done that job we have accomplished the job we have set out to do.

H.M.Jr: May I put it a little bit differently? May I just

- 23 -

put it a little bit - I mean this isn't what - I'm not stating what I think the problem is, but what I think the problem is that the President has in his mind, see? - that he gave us to study, see? I mean that doesn't mean that I say it is. But I'm going to try to just restate...

Oliphant: What he had in mind.

H.M.Jr: ...more or less what you said and see if we're together on that. As I understood it, what he asked us to study was the so-called - what some people call "hot" money, "bad" money, and various kinds of money, which flows from one country to another in times of stress, either for safety or for profit. Well, it's....

Eccles: Or current income.

H.M.Jr: Or current income. But it's that money which moves quickly...

Oliphant: It's "times-of-stress" money.

H.M.Jr: ...in times of stress.

Golden.: Well, that's different from speculative. That isn't the speculative element. It is the money that runs - owing to the present economic set-up of the world, is seeking refuge in America.

H.M.Jr: Well, it's that thing. Some people call it "hot" money, some people something else. But it's money coming here at this time because they think it is - the London stock market has passed its peak and they can make more money over here, or they are afraid of the European situation.

Eccles: There is an exchange speculation too in the case of...

H.M.Jr: Well, not so much. At any rate it's being driven here because it's in times of stress. As I get it, he wanted us to study whether we could slow down that movement, and that is the problem as I saw it, see?

- 24 -

- Golden.: That's the way I see it too, Mr. Secretary.
- H.M.Jr: I don't say that that - but that is what he asked us to study. Isn't that the way you would put it, Marriner?
- Eccles: That's what he asked us to study, that's right.
- H.M.Jr: And the further I go into the thing, talking now for myself, the more difficult I think it is to handle that kind of money without handling all the money that comes here. I mean I just don't see how you can take that kind of money unless you hit it all.
- Eccles: It is difficult to classify it. You've got a twilight zone in there that you just can't define.
- H.M.Jr: And then when you talk about it and other people raise the question of Scottish trusts and all that kind of stuff - but when you're going to level the wall and try to single out that money that comes here in times of stress, it is awful hard not to have a brush which is so big that it paints the whole canvas. And that, I guess, is why this is the fourth month we've been at it and haven't got anywhere.
- Green: Well, of course, a transfer tax, if we limited it to that, wouldn't necessarily deter money that is placed here for safekeeping; that is, distress money that is just put here as a safe place to put it because of the present European situation. They'd put it in a stable bond and forget about it until they needed it.
- H.M.Jr: Well, of course, Mr. Green, the great trouble is that a lot of the suggestions that have been made here by, if I may say so, the people outside the Treasury, have overlooked the administrative difficulties of enforcing it. Just the way I can sit here and make suggestions to you; I haven't made a study of exchanges and you can say, "Well, it's very nice, Mr. Morgenthau, but unfortunately you're just going to close the New York stock exchange if you do that, and you're just going to transfer the business to London." And I think we've each got to

- 25 -

give the other fellow a chance to say, "Well, if you suggest that, can it be enforced?"

Magill: I'm supposed to have a conference in there, so if you'll excuse me...

H.M.Jr: Let's wind it up; I won't let you go. Mr. Bell has a conference - I mean you (Magill) have a conference, so - I mean haven't we gone as far as we can? And take Magill's suggestion; just don't tear his memorandum apart, but see whether anybody else can come back with something which is as good or better.

Magill: And don't necessarily make it a tax.

H.M.Jr: All right, can we adjourn so Mr. Magill can go to his next conference?



THE SECRETARY OF THE TREASURY
WASHINGTON

MEMORANDUM FOR THE PRESIDENT

If the proposal for an increase in the rates of withholding tax, as originally submitted, is not acceptable, then the following substitute or supplementary plan is submitted for consideration:

Impose a tax on the transfer of corporate securities by or to a foreigner at a rate based upon a percentage of the sales or purchase price. To achieve flexibility, a minimum and maximum rate should be prescribed and the power given to the President, on the basis of designated finding and proclamation, to fix the effective rate. The operation of the tax will be substantially the same as in the case of the present transfer tax on corporate securities.

The broker, agent, or other person acting for the buying or selling foreigner in the execution of the purchase or sale would be responsible for the collection of the tax. Within the United States on the established exchanges, where the bulk of the transactions will take place, the tax would be effective. Transactions occurring outside of the exchanges, however, would present difficult problems (particularly in the case of bearer certificates or certificates in "street" names). The tax would tend to increase the number of the latter transactions but this would perhaps not endanger the objective since most of the business is and would remain in the hands of responsible brokers who would not seek the avenue of evasion with its prospective penalties.

- 2 -

The operation of the tax within the United States will tend to create a premium on American securities available for sale abroad without the payment of the tax. The tendency would be for citizens and resident aliens to attempt to obtain the benefits of this advantageous market by sending their securities to Canada or abroad. The following steps may be taken to check any such flow of securities from the United States to Canada and Europe:

(1) The American citizen or resident alien who sells or purchases securities of a domestic corporation outside of the United States would be made liable for the tax with heavy penalties for nonpayment. There would be a presumption in such case that the other party to the transaction was a nonresident alien. Discovery of the transaction would not be certain but the ever present possibility of detection, through examinations in connection with the income tax and returns of information filed by third persons, would be a powerful deterrent.

(2) Penalties would be provided for any domestic corporation (or its registrar) which recorded on its books the transfer of any security from or into the name of an alien, unless the tax thereon had been fully paid.

In the administration of the tax, the principal fact to be determined will be whether the purchaser or seller is a foreigner. The identity of the particular foreigner will not be in question. Hence, the operation of the tax will not be impeded by the prohibition placed upon originating foreign brokers who are usually subject to laws or usages prohibiting disclosure of the identity of the principal.

TREASURY DEPARTMENT

274

INTER OFFICE COMMUNICATION

DATE

February 25, 1957.

TO Secretary Morgenthau
FROM Herman Oliphant

For your information -

Control of Foreign Capital - Goldenweiser, Gardner, Bryan, and Green came on into my room for a further discussion. When they left, they seemed to be agreed on the following:

1. That the money we want to reach is not so much the daily traders' money, long-term investors' money, or panicky money, but what we agreed to call, for purposes of discussion, "recent wise money" coming here for a number of reasons including relative safety and semi long-term profits.
2. That we did not want to reach all of this money but only so much of it as would be necessary to stop or reverse the gold flow.
3. That the only question remaining open was not whether there should be a transfer tax, as opposed to some other kind of tax, but how high the maximum rate to which the President could raise the *transfer* tax should be in order to enable the President by gradually raising it to stop the amount of "recent wise money" necessary to stop or reverse the gold flow.



February 25, 1937

Excerpt from Mr. Magill's memorandum to the Secretary, "Memorandum of the Day's Activities February 25th:"

2. Non-resident aliens

Mr. Oliphant and I worked over the memoranda to the President regarding the proposed transfer tax. I also have memoranda from Mr. Haas, showing the character of the foreign investments in the United States (a very attractive colored picture) and the rates of transfer taxation in the principal foreign countries which are making investments here.

Mr. Wayne Taylor's friend, Mr. Raffalovich, spent a half-hour with me this morning, pointing out the dangers of retaliation by foreign countries if we should decrease the price of gold to foreigners or increase rates of taxation. He mildly suggested the imposition of a capital gains tax upon foreigners,- I suspect because he felt reasonably sure that such a tax would not be very effective.

"Hot Money" vs.

Frozen Funds

BY

FRANCIS P. GARVAN

President, The Chemical Foundation, Incorporated

THE DESERTED VILLAGE

No. **12**

American Political Economy

Compliments of

THE CHEMICAL FOUNDATION, INC.
654 MADISON AVENUE
NEW YORK, N. Y.

"Hot Money"

vs.

Frozen Funds

BY

FRANCIS P. GARVAN

President, The Chemical Foundation Incorporated

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Studies in Arithmetic

1. The Primer
2. A Second Primer
3. "Hot Money" vs. Frozen Funds.

PRINTED IN U. S. A.
FEBRUARY, 1937

FOREWORD

To the People of the United States of America:

The Chemical Foundation was founded by President Wilson for the "Promotion of Chemistry and Allied Sciences."

Eighteen years of our experience have demonstrated to us that arithmetic is the first of the sciences and the ally—in fact, the foundation—of all the sciences.

Our experience has also demonstrated that arithmetic is the most neglected science in America and that the effect of that neglect has been, is, and will be disastrous.

At long last, therefore, we are carrying on a campaign—in the grammar schools, secondary schools and colleges, and among our people in general—to repair this neglect.

The first and greatest neglect is the absolute failure to apply arithmetic to our international relations—and it is necessary to repair the leaks of a house before the family within can properly conduct its domestic affairs.

We are therefore sending to you an arithmetical study of our investments abroad, authorized by

us and made up for us by Pasley & Conroy, a firm of American accountants of the highest standing. It is the best that the inadequacy of government collection of data affords. Wherever possible the government's inadequate figures have been supplemented, checked and corrected.

We invite comments and criticism, friendly or unfriendly, particularly on the subject—What is the real value of these foreign investments, in view of conditions in the world today?

This report states that our foreign investments are estimated at some Eight Billion Eight Hundred Million Dollars, using market values where they can be obtained and book values in all other cases.

This is the estimate of what is remaining of a Fifteen Billion Dollar investment (excluding war debts). What is its realizable value? What is its "hot money" value?

Some Two Billions represent the remains of our unhappy venture into foreign government loans. What will we eventually realize?

We have a billion dollars invested in public utilities. Can we object to confiscatory legislation by foreign governments in the face of our own government's attitude toward private utilities? What is the real value of these investments?

We have a billion dollars in oil. The record of recent foreign legislation affecting this invest-

ment is discussed in this report. Spread out all over the world, subject to the legislation of many governments, what is it worth? What would be the cost to the nation of protection against confiscation?

We have a billion dollars in mining. This, too, is scattered throughout the world, subject to the same perils as our oil investments. What is it worth?

What is the value of investments in war-torn Spain, in Germany, and other continental European countries, now figured at book value where there are no market values available?

We have a half billion dollars invested abroad in agricultural and paper and pulp ventures. Is it more expensive for us, as a nation, to legislate benefits to Cuban sugar and Canadian paper—to protect our investments in these industries—or would it be cheaper for us, as a nation, to build up home industries?

Take these foreign investments to your banker and ask him how much any sound bank would loan on them.

These are but a few of the questions to be considered in placing the real value on our investments abroad.

Let us now look at the other side of the Balance Sheet. Foreign investments in this country, according to an official statement issued by

Secretary Wallace on February 8, 1937, amounted to Seven Billion Dollars. This undoubtedly is based on all figures available to the government at the present time.

The government bases its figures on information furnished voluntarily in answer to questionnaires sent to all those who it thinks might have information. Under this system, a substantial amount of its information must come voluntarily from the agents of the foreign investors. Its estimate, therefore, is dependent on what information foreign agents wish it to have.

This is a wretched method. My experience as investigator of concealed German property during the World War and as Alien Property Custodian from 1919 to 1921, amply justifies me in saying that the figures gathered in this manner cannot represent more than 75% of the foreign investment here.

I, therefore, am confident that it amounts to over Nine Billions of Dollars. But we have no right to go on doing business on this basis.

All studies of our international balances will be hopelessly inadequate and incomplete, and policies based on our present figures will be necessarily unsound, until a law is passed compelling the contemporaneous report, under oath, of present foreign investments and thereafter of every foreign transaction, contract or agreement, and

until business machines make these true figures available to our people by the fifteenth of the ensuing month. Until that time, we will do the best we can and ask the help of every one.

However, it is not merely a question of matching dollar values. Must we not also consider the value to the foreign nations of the power—economic and political—wielded over us by their foreign investment here? Do they not control our stock markets? Do not their agents here control our banks? How far are Lord Rothermere and Lord Beaverbrook, in command of the price of newsprint, able to control the trend of popular opinion by the threat to our press of a return to \$120 a ton for newsprint? What is the value of the power of control over our necessities—rubber, tin, coffee, tea, nickel, and manganese? What is the value of the power of England over the gold supply of the world? What was the power of the German control over us, exercised by her investments here, on the chemical, drug and dye industries from which, happily, after twenty years' effort, we are now free?

What American would not gladly exchange the Eight Billion Eight Hundred Million Dollars that we have scattered all over the world, subject to the legislative whims—not of one government—but of all the governments of the world, subject eternally to revolution, dictatorships, wars,

national animosities, special taxation, manipulated currencies, etc., for the Nine Billions of foreign investments in America?

Are we not, in truth and in fact, a debtor nation?

Respectfully submitted,

THE CHEMICAL FOUNDATION, INC.

By

Francis P. Garvey
President.

EXHIBIT "A"

An Estimate of American Long-Term Investments Abroad as at December 31, 1936

Foreign government and government-guaranteed bonds, after estimated repatriations—at market values	\$2,224,850,000	
Foreign corporations—stocks and bonds—publicly owned:		
Stocks—at market values	\$1,477,343,000	
Bonds—at market values	676,482,000	2,153,825,000
American corporations, all or substantially all of whose assets and activities are abroad. Securities issued and outstanding priced at market ..		1,380,249,000
Investments of American corporations abroad, through wholly-owned or majority-owned-and-controlled foreign subsidiaries. Book values as at December 31, 1935 (See Note 1)		3,053,722,000
<i>Total Value of American Long-Term Investments Abroad at December 31, 1936</i>		<u>\$8,812,646,000</u>

NOTE 1. As stated above, no market values were obtainable for investments in the amount of \$3,053,722,000. Book values as at December 31, 1935, are used.

Due to lack of information no estimate is made of any appreciation or depreciation in their value for the year 1936. It is believed that new investments and reinvested net earnings substantially offset sales.

PASLEY & CONROY
CERTIFIED PUBLIC ACCOUNTANTS
MEMBERS OF AMERICAN INSTITUTE OF ACCOUNTANTS

67 WALL STREET
NEW YORK

ROBERT S. PASLEY, C.P.A.
THOMAS F. CONROY, C.P.A.
JOHN P. BARLOW, C.P.A.
JOHN A. SMITH, C.P.A.

February 5, 1937

MR. FRANCIS P. GARVAN, *President*
The Chemical Foundation, Inc.
654 Madison Avenue
New York, N. Y.

Sir:

Pursuant to your request we have made an investigation and study of American Long Term Investments Abroad and in connection therewith submit the following:

- Exhibit A* An Estimate of American Long Term Investments Abroad as at December 31, 1936.
- Exhibit B* An Estimate of American Long Term Investments Abroad as at December 31, 1935, with nine schedules.
- Exhibit C* An Estimate of American Long Term Investments Abroad as at December 31, 1935, distributed geographically.

[1]

The estimates submitted herewith have been prepared by us from data accumulated from sources set forth below, and the method and valuations used are stated hereinunder.

Sources of Data

In the preparation of the statistics furnished herewith there was compiled a record of all known corporations and individuals that may have had foreign interests at one time or another. This list was obtained by combing all known sources of data and the data so accumulated were brought up to date by reference to the latest published records. There is submitted below a partial list of publications examined. In addition, considerable information was obtained through conversations with and inquiries made of corporation officials, trade associations, bankers, brokers and organizations having special knowledge regarding some particular industry or company engaged in foreign operations.

Holdings of individuals or close corporations, not otherwise obtainable, have been provided for by omission estimates. The portfolios of American investment trusts and other financial institutions were scrutinized and any foreign holdings not already provided for were extracted and inserted in their proper industrial location.

[2]

Sources of Data

- * Moody's Manuals
- * Poor's Manuals
- * Corporation reports to stockholders
- * Registration statements filed with the various stock exchanges under the Securities and Exchange Commission regulations
- * American Underwriting of Foreign Securities—U. S. Dept. of Commerce
- * American Direct Investments in Foreign Countries—U. S. Dept. of Commerce
- * Balance of International Payments—U. S. Dept. of Commerce
- * Canadian-American Industry—Marshall, Southard & Taylor
- * Dominion Bureau of Statistics
- * Survey of Corporate Securities—Financial Post
- * Commercial and Financial Chronicle
- * The Economist—London
- * Yearbook—American Bureau of Metal Statistics
- * Foreign Policy Assn.
- * World Petroleum Directory
- * The Petroleum Register
- * Manual of Sugar Companies—Farr & Co.
- * Foreign Dollar Bonds—White, Weld & Co.
- * Foreign Dollar Bonds—Iselin & Co.
- * N.R.A. reports
- * Report of the Superintendent of Insurance—Dominion of Canada
- * Copper—National Industrial Conference Board
- * Ontario Bureau of Mines
- * Philippine Government Bonds—C. J. Devine & Co.
- * Fortune
- * Federal Reserve Bulletins
- * Federal Trade Commission Reports
- * Various U. S. Senate documents
- * Miscellaneous financial magazines
- * Various newspaper reports
- * Miscellaneous publications of the U. S. Dept. of Commerce

* Various reports of various years.

[3]

Method of Valuation

It appears to us that an accurate appraisal of our foreign investments should be based wherever possible on market values; that an estimate based on par values or acquisition costs conveys a misleading impression and is not representative of true value. It is obvious that any estimate which valued Imperial Russian Government bonds or Mexican National Railway bonds at their original cost to us would be misleading. True, estimates made in the past have provided for certain inaccuracies, such as these, resulting from the use of book values but many other overstatements have gone on without adjustment. The fact that we are considering here investments of the entire nation does not change the basic truth, that a true statement must be based, wherever possible, on market values.

Estimates of our foreign investments, in the past, have been divided between those classified as "Portfolio" and "Direct." The line of demarcation is very fine and serves no practical purpose. As the Department of Commerce observed in its 1929 survey:

"'Direct investments' and 'portfolio investments' overlap. American corporations often finance their direct investments by the public sale of securities."

The division made here disregards the classifica-

tions "Portfolio" and "Direct" used by the Department of Commerce, and more closely follows the divisions used by Sir Robert Kindersley in his survey of British "overseas" investments.

Accumulation and Presentation of Data

The entire field was divided into the eight most significant and related types of industrial activity. This grouping is very similar to that used in estimates prepared by the Department of Commerce. A departure, however, has been made in the case of holdings of foreign corporation bonds which are included, in the statements submitted herewith, in the proper industrial classification, and not with foreign government bond issues, usually termed "portfolio."

After completing the industrial allocations, the investments were then divided into four distinct classifications:

1. American holdings of the bonds of foreign governments, their political subdivisions, and government-guaranteed issues.
2. Foreign corporations, publicly owned, in which Americans (individuals or corporations) have an interest. Such interest includes stock and bond ownership either of a minority or majority character.
3. American corporations, all or substantially all of whose assets and activities are abroad.

4. Investments abroad of American corporations through wholly owned or (51%) controlled foreign subsidiaries.

No deduction has been made for foreign holdings of securities of American corporations, all or substantially all of whose assets are abroad, as foreign holdings of these securities are customarily considered as foreign investments in American securities.

We comment on the items comprised by Exhibits "A" and "B" and supporting schedules as follows:

An Estimate of American Long-Term Investments Abroad

The basic data accumulated in this study were as of December 31, 1935. Detailed information as of the end of 1936 particularly with respect to investments by American corporations in foreign subsidiaries will not be available for some months.

As set forth on Exhibit "A" submitted herewith, the value of our long-term investments abroad at December 31, 1936, was estimated at \$8,813,000,000. Of this total, \$5,759,000,000 represents market values. It is pointed out here that the principal market for the great majority of our foreign investments is in this country, and, therefore, as to most of these securities, market values represent values placed on these securities by Americans—not foreigners. The remainder—

\$3,054,000,000—represents book values of investments in companies whose securities are closely owned and for which no market quotations were available. These book values are as of December 31, 1935, as sufficient data are not available to compile an estimate of book values at December 31, 1936. From such information as is at hand, however, we believe that no substantial change has occurred therein during the year 1936.

During the year 1936 market values of those investments abroad for which market prices were obtainable increased in the substantial amount of \$780,000,000. Net receipts from further liquidation of our holdings of foreign government and government-guaranteed bonds and foreign corporation stocks and bonds resulted in an inflow of funds estimated at \$196,000,000, resulting in all in a net increase during the year 1936 in the value of those investments abroad for which market values were obtainable in the amount of \$584,000,000.

There is set forth on Exhibit "B" a statement of the value of our long-term investments abroad at December 31, 1935, which at that date were placed at \$8,228,000,000. The Department of Commerce in its Bulletin "The Balance of International Payments of the United States in 1935" estimated our investments abroad at December 31, 1935, at \$12,630,000,000. The discrepancy between the two estimates is principally due to the

following:

Market Values used by us as substitution for Book Values	\$2,289,000,000
Difference in estimate of Par Values of "Portfolio" Investments outstanding, and the amount thereof in American hands after deducting estimate of repurchases by foreigners	847,000,000
Difference in Book Value of "Direct" investments principally due to operating losses, write-downs through reorganizations, bankruptcies, etc., during depression; also difference due to decline in Market Values of foreign stocks, discussed hereinafter	1,267,000,000
Total	\$4,402,000,000

The Department of Commerce estimated "Portfolio Investments" outstanding at par value of \$5,895,000,000 before repurchases, and at \$4,795,000,000 after repurchases. The comparable figures entering into our study, as far as we can ascertain from data published, are \$5,770,000,000 before repurchases and \$3,948,000,000 after repurchases. In a study "America's Experience as a Creditor Nation" by Messrs. Madden, Nadler and Sauvain, they estimated American holdings of foreign dollar bonds at the end of 1935 (Table 39, page 198) at \$4,129,957,000 and stated:

"This compares with the Commerce Department's estimate of \$4,795,000,000 for total American portfolio investments abroad."

In our study, we have excluded, in so far as possible, those foreign bond investments of United States life insurance companies held by the Receiver General of Canada to cover the actuarial liability of those companies to Canadian policy-

holders. The total of such investments approximates \$400,000,000.

The Department of Commerce has qualified its December 31, 1935 estimate of "Direct" investments abroad by stating that such estimate "can be considered as only approximate until a new detailed study has been made." Its last complete reported study of direct investments was as of the end of 1929. The huge losses in book values resulting from the many bankruptcies, reorganizations and write-downs during the depression years do not appear to have been fully reflected in the adjusted estimates of the Department of Commerce in recent years. These estimates, as will be noted from the following table, indicate that the losses in excess of reinvested earnings, based on the 1929 survey, were \$171,000,000, and, as based on its 1930 "New Estimate," \$351,000,000.

Dept. of Commerce 1929 estimate, adjusted to include omission of bank capital	\$7,603,000,000
Net additional investments 1930-1935 inclusive (Bulletin No. 833, Table XVII)	403,000,000
Total investment	\$8,006,000,000
New estimate	7,835,000,000
Difference	\$ 171,000,000
Dept. of Commerce 1930 estimate	\$7,966,000,000
Net additional investments 1931-1935 inclusive (Bulletin No. 833, Table XVII)	220,000,000
Total investment	\$8,186,000,000
New estimate	7,835,000,000
Difference	\$ 351,000,000

Our study develops that in agricultural investments alone book values have shrunk \$400,000,000 since 1929. The reduced volume of export trade has also brought about a substantial decline in the number of sales agencies abroad. Manufacturing plants and other industrial investments have suffered greatly in countries with blocked exchanges. Our study has indicated that these losses, since 1929, have totaled over a billion dollars. There is also to be considered the decline in market prices since 1929 where such basis was used by the Department of Commerce in its 1929 survey. To quote from Bulletin No. 731, page 4:

"Where the investment was one of partial ownership of the stock of the foreign company, the market value of the holding was requested—on the assumption that the market value would, to some extent, reflect the surplus or deficit position of the company more clearly than the par value of the stock. Although some companies reported the market value as of September, 1929, this value was not accepted, because for many stocks it represented the highest value reached by a very speculative market. All such returns were changed to the market values as of the end of December, 1929. Where the stock of the foreign subsidiary or corporation was closely held, or for some other reason not listed on any stock exchange, it was necessary to use its par value."

The decline in market value of our investment in Canadian Pacific stock (valued at market by

[10]

Dept. of Commerce) since 1929 amounted to approximately \$150,000,000.

There are many other factors which have tended to reduce our foreign investments. Briefly they are:

(1) The constantly diminishing percentage of American ownership in Canadian enterprises. International Nickel, Bell Telephone of Canada, Canadian Pacific Railway are some of the larger companies involved. (See "Canadian American Industry," p. 326, by Marshall, Southard & Taylor for list of smaller companies repatriated.)

(2) The almost complete repurchase by Europeans of the "American shares" of European corporations of which large amounts were floated here in the years 1926 to 1929. The most prominent instances are Belgian National Railways Pfd., Carreras, Ltd., Swedish Ball Bearing Co., Austrian Credit Anstalt, Banca Commerciale Italiana, Hungarian General Savings Bank, Hungarian Discount & Exchange Bank, Mercurbank of Vienna, Mortgage Bank of Colombia, Snia Viscosa, Isotta Fraschini, Rolls Royce, Ltd., Pirelli Co. of Italy, Fiat Co., North German Lloyd, and Holland American Line.

(3) The diminishing number of outstanding bonds held by Americans in those foreign enterprises which have been considered by the Dept. of Commerce as "Direct" investments.

[11]

History of Direct Investments Abroad During Recent Years and Status by Industrial Divisions at December 31, 1935

There are submitted, in the following chapters, statistical data and observations gathered during the course of this study. These comments are made by industrial groupings.

Railroads

American investments in foreign railroads at December 31, 1935, are estimated at \$466,188,000 at book values, and \$312,568,000, substituting market values where obtainable (see Exhibit "B," Schedule 2). Only steam railroads are included in this classification. Electric and street railways are included under "Public Utilities." A small amount of steamship company holdings wherever they can be construed as being of the transportation type are also included.

American Corporations, All or Substantially All of Whose Assets Are Abroad

There are only a few companies included in this classification, the largest being International Railways of Central America, Cuba Company, Guantanamo & Western, Philippine Railway, and Mexican Northern Railway.

[12]

Our investment in Cuban railroads is confined principally to the Cuba Company. The sugar plantations held by the Cuba Company, through its subsidiary Compania Cubana, have been excluded and have been valued in the agricultural section of this report. The Cuba Company is in reorganization, and its securities were selling at December 31, 1935, at about 26% of the book value of the company. Its revenue is principally derived from the sugar industry, directly or indirectly. There is a large foreign interest in this company.

It is interesting to note that with respect to certain of our railroad investments abroad, the payment of interest and dividends on outstanding securities held by Americans need involve no transfer problem. For example, the International Railway of Central America receives a large part of its income from the business of freighting bananas for the United Fruit Co., another American-owned and controlled enterprise. It may be possible that, if desired, payments for such services could be effected in the United States as both companies have their head offices here. The identical problem is presented by the Cuba Company which does a large business with American sugar companies operating in Cuba. This company also has its head office in New York.

The total book value of our investment in American-owned railroad companies operating

[13]

entirely abroad is estimated at December 31, 1935, at \$187,772,000; market values at \$52,416,000.

American Corporations Having Wholly-Owned or (51%) Controlled Foreign Subsidiaries

The total value of these investments is estimated at \$82,294,000, representing book values. There are no market valuations obtainable. However, it appears that the book values of these properties are far in excess of their actual values.

The largest investment in this category is the Mexican branch of the Southern Pacific Railroad, operating about 1,500 miles of trackage in Mexico. This investment has experienced the same general decline as other American investments in Mexico, such as oil and copper. What its actual value is, from an income or liquidating basis, is merely conjecture. It is extremely doubtful that this property is worth the value of approximately \$35,000,000 stated on the company's balance sheet (using the 3.55 rate of conversion, which is the rate used by the parent company in consolidating the peso accounts).

Another large investment in this section is that of the New York Central Railroad in Canada. Approximately 1,026 miles of road are operated in the provinces of Quebec (90) and Ontario (936). The largest single item included here is that of the Canada Southern Railway Co. which has been leased to the Michigan Central Railroad for 999

years, dating from 1904, and now subleased to the New York Central. The rental consists of a bond interest guarantee and a 3% dividend rate for the common stock, which in turn is partly owned (55%) by the New York Central Railroad. The outstanding bonds of the Canada Southern, estimated in American hands, totaling \$17,500,000, are included with American holdings of foreign corporation bonds.

Other holdings include those of the Great Northern Railway, Delaware & Hudson, Northern Pacific and the Pere Marquette Railroad. They are all located in Canada.

Foreign Corporations Publicly Owned in Which Americans (Individuals or Corporations) Have an Interest

The amount of these investments is estimated at December 31, 1935, as follows: stocks, at market, \$38,045,000; bonds, face value, \$158,077,000, market value, \$139,813,000.

The principal holding here is our investment in Canadian Pacific. The annual report of the Canadian Pacific Railroad (1935) states that 24% of the common stock and about one-half of 1% of the preferred is held in the United States. Our holdings of bonds in this company are far greater in value and have been estimated by us at \$86,800,000 face value; at market value, \$88,000,000. The next largest investment is in bonds of the

Canada Southern amounting to \$17,500,000 at face value, and \$19,600,000 at market. The remainder consists mainly of holdings in Belgian National Railways, various French railways, North German Lloyd, Canada S. S. Lines, and investments, some of a private nature, in certain South American railroads.

Our investment in bonds of Canadian National Railways is included under "Foreign Government and Government-guaranteed Issues." These bonds are guaranteed by the Canadian government.

Public Utilities

Our total investments abroad in public utilities, at December 31, 1935, are estimated, at book values (as shown by Exhibit "B," Schedule 3), at \$1,518,286,000. Investments having a book value of \$1,375,860,000 had a market value of \$787,072,000 indicating a loss, at market, of \$588,788,000. Investments for which market values were not obtainable, representing investments of American corporations in wholly owned or 51% owned and controlled foreign subsidiaries, totaled \$142,426,000.

Our greatest losses as measured by the difference between book values and market values have been incurred in public utilities. It is important to note that with respect to these companies, their activities do not interrelate with our domestic

[16]

economy. They neither produce here and sell abroad nor produce abroad and sell here. The result has been that they are particularly affected by transfer problems.

This is borne out by the experiences of two American corporations representing a substantial amount of our public utility investment abroad—the American & Foreign Power Corp. and International Telephone & Telegraph Co. Based on a comparison of book values with market values (adjusted for value of assets in the United States) our loss as to these two investments amounted, at December 31, 1935, to more than \$400,000,000. The decline in value of these investments has been due not only to loss of revenue, because of the general world-wide depression, but also to various restrictions imposed on the companies by certain foreign governments. In Chile, for example, where the American & Foreign Power Corp. has huge investments, the control of the properties has passed into Chilean hands. This was done in settlement of certain large fines imposed on the company for violation of the Chilean exchange control laws. In addition, two-thirds of the earnings of the property go to the Chilean government, one-half of which is applied to the reduction of the cost of electricity to consumers. One of the major problems of the American & Foreign Power Corp. is that of restricted dollar income due to exchange embargoes

[17]

and the fluctuating and unstable currencies of the countries in which its subsidiaries operate.

An adverse factor arising during 1936, affecting the International Telephone & Telegraph Co., is the civil war in Spain, where the company has approximately \$67,000,000 invested. Regardless of protestations of both warring factions regarding the inviolability of foreign properties, there is no doubt that the International Telephone & Telegraph Co. investment in Spain is not worth \$67,000,000 today. Current news items tell the story graphically. It may be years before the International Telephone & Telegraph Co. can show earnings received in the United States from its Spanish subsidiary. This company also has some \$14,000,000 invested in Germany. As matters stand today, all of our German investments are really nationalized. Germany enjoys the benefit of our capital investments there, but at present we receive no return on them.

Another unfortunate foreign investment is that of the Intercontinents Power Corp. in Argentine, Brazil, and Chile. This company has been ruined by currency restrictions and currency depreciation. At December 31, 1935, the company's securities were valueless.

American Corporations Having Wholly-Owned or (51%) Controlled Foreign Subsidiaries

The total book valuation of these investments is estimated, at December 31, 1935, at \$142,426,000.

[18]

The majority of these investments are located in Canada—approximately \$75,000,000. The largest Canadian investments are those of the International Hydro Electric System, International Utilities, Cities Service, Middle West Utilities and Niagara Hudson Power. In Europe, our only sizeable investment at December 31, 1935, was the Utilities Power & Light in England, which was disposed of by sale during 1936. In the Far East, our investments are found mostly in the Philippines, in companies such as Manila Electric, Islands Gas & Electric, and Manila Gas.

Foreign Corporations Publicly Owned in Which Americans (Individuals or Corporations) Have an Interest

The total of our investments in this section is estimated, at market prices December 31, 1935, at \$427,292,000; \$86,028,000 in stocks, \$341,264,000 in bonds (face value of the bonds, \$426,972,000). It is interesting to note that our investments in foreign controlled public utilities have fared much better than those foreign investments which are controlled by Americans or American corporations. This is partially due to the preponderance of Canadian corporations in foreign-controlled investments, whereas, with respect to American corporations operating abroad, the investments are located principally in Latin America and Europe.

[19]

Our largest investment in Canada is in the Bell Telephone Co. of Canada. Approximately 29% of the common stock of that company is owned by Americans or American corporations. The American Telephone & Telegraph Co. has a one-fourth interest in the company. However, our holdings of Bell Telephone of Canada bonds are even larger in value, being estimated at \$31,750,000 face value, and \$36,470,000 market. Holdings in other large Canadian public utilities are found principally in the form of bonds. Approximately \$132,000,000 at face value are invested in Gatineau Power, Saguenay Power, and Shawinigan Water & Power Co., Ltd. Other Canadian enterprises that have attracted American investors are Montreal Tramways, Montreal L. H. & P. Cons., Power Corporation of Canada, and Manitoba Power. Our investments in these companies, and as a general rule in all Canadian public utility companies, have fared about the same as investments in similar domestic securities. There have been very few defaults.

Our investments in European public utility bonds have been unprofitable. This is due to the preponderance of German public utility bonds. All German bonds are in complete default and are selling at about 20 cents on the dollar. The outlook is dark for any future resumption of interest and as these bonds have been and are being repatriated in considerable amounts, the oppor-

tunity to recover part of our loss is very limited. Other large European bond investments are in Italy and the Scandinavian countries. They are being serviced in full. Certain Italian stock investments, however, show a large depreciation in value and return very little in the way of dividends. The Italian currency transfer restrictions have had a serious effect on the earnings and cash position of the United States parent companies, notably Italian Superpower and International Power Securities.

In the Far East, American funds are invested principally in corporate bonds of the Nippon Electric Co., Great Consolidated Electric Power, Tokyo Electric, Toho Electric Power, Shineytsu Electric Power, and Ujigawa Electric Power. Our investment in bonds of Taiwan Electric Power is included under "Foreign Government and Government-guaranteed Issues."

With respect to public utility investments, it would appear that the expansion of public utilities in many countries has been too far ahead of the economic development of such countries.

Agriculture

(Excluding Rubber Plantations)

American investments in agriculture are confined principally to our holdings in the fruit and sugar industry spread throughout Latin and

South America. The decline in the value of our investments in this field has been proportionately greater than in any other field of investment. This is especially true of the sugar investments in Cuba and the West Indies. Practically all of the companies involved have gone through reorganizations and some have been permanently dissolved.

At December 31, 1929, the Department of Commerce estimated all agricultural investments (excluding rubber) at \$831,860,000 which, at the end of 1935, had shrunk to \$431,059,000 book value. Even this does not present the true picture of the decline in such investments for, of \$265,856,000 of such book values, the market value was only \$63,469,000. As to the remainder, the market value was unobtainable. At December 31, 1935, our investments in sugar companies showed a decline in book value, from December 31, 1929, of approximately fifty percent (50%).

It is important to note that the successful operation of these companies is predicated to a great extent on the market afforded by ourselves for foreign products which compete with our own home-grown agricultural products. It is only since the recent tariff concessions, granted by the United States in the reciprocal trade treaty with Cuba, have been in effect that the Cuban sugar industry has staged a come-back. In 1934 Cuban sugar supplied 25% of all the sugar consumed in

the United States, and Philippine sugar 18%, close to one-half of our total sugar requirements. In 1936 approximately 2,000,000 tons of Cuban sugar were marketed in the United States out of a total production of 2,600,000 tons. The balance is sold in other foreign ports at a distinct loss. Recently the New York market for Cuban sugar was quoted at 2.85 cents a pound before duty, against less than a cent a pound in London at the same date. Americans have invested probably close to three-quarters of a billion dollars in Cuban sugar enterprises and at December 31, 1935, this three-quarters of a billion had shrunk to less than \$100,000,000, a loss of over 85%.

From the standpoint of the Balance of International Payments of the United States, certain observations can be made. Sugar exports to the United States by companies that are American owned and controlled do not necessarily involve transfer of the full import value to Cuba by the importer in the United States. Dollar balances built up from the sale of the sugar in the United States need be drawn on only for payments in Cuba of operating expenses incurred in the conduct of the company's business there. Any interest or dividends paid out to Americans holding securities in these companies would likewise be paid out of these funds. Therefore, these companies are not faced with an exchange problem when paying interest and dividends on their securities.

This is also true of the activities of the fruit companies. The United Fruit imports bananas from its own plantations in Central America and sells them in the United States. The amount of funds actually remitted to Central America need not bear any relation to the value stated in the import statistics. The same situation arises with respect to those American companies which have sugar properties in Cuba, which properties merely act as feeders of raw materials needed in the manufacture of their products in the United States.

Included among our agricultural investments abroad are certain Canadian sugar corporations, operating in Cuba, in which Americans appear as either directors or officers. Such investments have been valued at the market prices of the shares estimated to be American owned. These investments are estimated at a little over three million dollars. The investment of Borden and other dairy companies in Canada, while their activities are partly manufacturing, have been included as agricultural. Certain small bond holdings of American investors in Canadian grain grower companies have been included. Holdings in Philippine sugar companies (notably the Calamba Sugar Estates) have been provided for. It is understood that a good portion of the Philippine sugar industry is owned by English capital. Certain small Hawaiian sugar companies with Philippine holdings have been included. An

[24]

omission estimate for unknown private holdings mostly in Canadian farms has been provided for.

Our agricultural investments in Mexico, formerly quite extensive, and consisting mostly of cattle ranches, are rapidly disappearing. Under the new Mexican agrarian program, all foreign agricultural properties are being confiscated as rapidly as possible, and payment is being made in Mexican bonds of doubtful value.

Summed up, between December 31, 1929, and December 31, 1935, there has been a loss in our agricultural investments abroad of over \$400,000,000 in book values and, substituting actual market valuations wherever possible, a total loss of over \$600,000,000.

Rubber Plantations

American investments in foreign rubber plantations are confined to a few companies.

At December 31, 1929, the United States Department of Commerce estimated these investments at \$50,000,000. There has been very little change since that date. At December 31, 1935, our investment in rubber plantations is estimated at \$40,945,000. The valuations included therein are all book figures except with respect to one small investment—a company operating in Mexico. The stock of said company is selling at about 25% of its book value.

[25]

Practically all of our investments in rubber plantations are in British Malaya and the Netherlands East Indies. As stated above, there is a small Mexican enterprise, now practically out of operation. Another plantation is in Liberia, Africa, the development of the Firestone Tire & Rubber Co. The Ford Motor Co. has an experimental station for rubber on the Amazon river. No estimate has been made for such development at December 31, 1935, as no data with respect thereto were available. The Goodyear Tire & Rubber Co. started rubber experiments in Panama in August, 1935, having acquired 3,000 acres for that purpose.

Investments in rubber plantations by the large American tire manufacturers were instituted with a view to providing them with a source of raw material and to free them from dependence on foreign-controlled rubber cartels. However, less than 10% of our entire crude rubber imports are produced by American-owned or controlled companies. In 1935, 1,045,000,000 pounds of rubber were imported at a value of \$119,081,000. We are still mainly dependent on foreigners for our rubber. The recent development of synthetic rubber in the United States may some day free us from such dependence, as has happened in the case of nitrates.

With respect to imports of rubber produced by subsidiaries of American corporations, the same

situation exists with respect to declared import value and transfer of funds as that discussed in the previous chapter with regard to sugar. The import value does not necessarily represent the amount paid. To quote from Poor's 1936 volume, page 1344, detailing the bookkeeping operations of the U. S. Rubber Plantations, Inc.:

"Rubber received from the plantations is taken into account by the U. S. Rubber Co. at current market prices and the plantation companies are credited in open account. *The plantation companies draw against this open account for current cash requirements.*"*

Paper and Pulp

Our foreign investments in the paper and pulp industry have been centered almost entirely in Canada and have largely been actuated by the necessity of supplying as cheaply as possible the tremendous demand for this product in the United States. The growth of the paper and pulp industry in Canada has been in line with the decline of our own forests and our increasing demand for pulp and paper. The prohibition on exports of pulpwood from crown lands hastened the erection of paper mills in Canada. The predominating impulse throughout has been the need of a new source of supply to offset the increasing

* Italics ours.

cost of paper from our own dwindling forest reserves in the north.

It can be said that the bulk of these investments were made because of the market afforded in the United States for the sale of pulp and pulpwood. The recent development of our southern slash pine may act as a deterrent on any future expansion northward. In addition certain restrictions placed on American paper concerns by the Canadian government may also have an adverse effect on any new investments in Canada.

As at December 31, 1935, our total investments in paper and pulp are estimated, using market values where obtainable, at \$207,422,000, and \$314,172,000 at book values.

American Corporations, All or Substantially All of Whose Assets Are Abroad

The total value of these companies is estimated at \$130,653,000 at book value, and \$57,101,000 at market. The loss in value at this date cannot be attributed to any adverse political actions. The price of pulp is the determining factor in the successful operation of any pulp concern. Practically all pulp mills in Canada and the United States have been forced into reorganizations or receiverships during the past six years due to the abnormally low price for pulp prevailing during that time. Recent rising prices for pulp and the rising demand due to the general economic improve-

[28]

ment during 1936 are reflected in the greatly increased market prices of the outstanding securities of these companies, which securities, during the year 1936, practically doubled in market values.

American Corporations Having Wholly-Owned or (51%) Controlled Foreign Subsidiaries

The total book value of these subsidiaries is estimated at \$110,391,000. No doubt, if the actual market values of these foreign properties had been obtainable they would have reflected somewhat the same experience as those companies for whose securities market values were available. However, some of these investments appear to have been made solely to provide a source of raw material to the parent companies and, therefore, were not as greatly affected by the fluctuating price of raw pulp or paper as companies selling their production in the open market. Examples of this type of investment are the holdings of the *New York Times* in the Spruce Falls Paper & Power Co., and the *Chicago Tribune* ownership of the Ontario Paper Co., Ltd.

Foreign Corporations Publicly Owned in Which Americans (Individuals or Corporations) Have an Interest

The market value of American ownership of shares at December 31, 1935, is estimated at

[29]

approximately \$3,156,000, and bonds at \$69,972,000 face value, worth \$36,774,000 at market values. The large depreciation again evidenced here has, as stated before, been due to the general economic depression influencing both the price and demand for paper and pulp.

Oils

The United States occupies a dominant position in world petroleum affairs, due not only to our own great petroleum development but also to our tremendous investments in foreign oil resources and distribution agencies. In this field we find that comparatively few companies do most of the business. The smaller companies engage principally in development work and leave the production, refining, and distribution to the large companies. Some of the smaller companies do produce oil, but sell their production to the larger companies.

American Corporations, All or Substantially All of Whose Assets Are Abroad

The book value of these investments at December 31, 1935, is estimated at \$120,544,000 and their market value \$51,992,000 or less than half. The large decline in valuation thus reflected is due principally to a few development companies, notably the Andes Petroleum, Leonard Oil Development, Carib Syndicate, American Maracaibo Oil,

[30]

Pantepec Oil, and Venezuelan Petroleum Co. Development companies usually place an arbitrary value on their acreage far in excess of its actual value. There are a number of possible reasons for such over-valuation: stock promotion, potential value, taxes, etc. The market prices of the securities of these companies provide a far more accurate valuation than the over-capitalized values as shown on the companies' books. There is included herein only one producing company of importance, the market value of which company's shares are in excess of book value. This is the Creole Petroleum Corp. which is controlled by the Standard Oil Co. (N. J.). Standard's holdings in this company (75%) are not included under this heading as they are included as part of that company's foreign investment.

American Corporations Having Wholly-Owned or (51%) Controlled Foreign Subsidiaries

Included herein are the holdings of the Standard Oil Co. (N. J.), our largest foreign investor. While its holdings of Imperial Oil, Ltd., Creole Petroleum, International Petroleum, and a few others, do permit of market valuations the majority of Standard's foreign investments are in companies for which no market values are obtainable. We have, therefore, used book value in estimating foreign investments of Standard Oil (N. J.).

[31]

The recent sale of the Standard's Argentine holdings to the government of Argentina because "the government's action made it impossible to operate on a commercial basis," shows clearly the uncertainties surrounding these foreign investments. Other recent items indicating a similar trend are: (1) The wide-spread agitation in Venezuela against foreign oil companies, in which sabotage and violence were employed by the agitators. The oil concerns have reduced their stored oil supplies 80% in fear of confiscation. Further, the oil companies have informed their employees not to bring their wives and children to Venezuela. American companies have probably close to \$200,000,000 invested in Venezuela. Only the most stringent measures by the Venezuelan government, assisted by military measures, have prevented the loss of this tremendous investment. What the action of any newly elected government will be is problematical in view of the temper of the electorate. (2) The oil strikes in Mexico have had a serious effect on foreign companies operating there. (3) The marked increase in taxes levied on oil companies in Colombia. (4) The action of the Japanese government requiring all oil companies to keep a six months supply of oil on hand, forcing construction of unneeded storage facilities.

There are other oil companies with large foreign investments. While not comparable to the

[32]

Standard Oil Co. (N. J.) they are, nevertheless, of great size and are spread throughout every nation of the world. Among the largest are Socony Vacuum, Texas Corporation, Gulf Oil, Standard of California, Consolidated Oil, Union Oil of California, Atlantic Refining, Seaboard Oil, Pure Oil, Tidewater Associated Oil, and Continental Oil.

The total valuation of this section is estimated—at book values—at \$986,557,000.

Foreign Corporations Publicly Owned in Which Americans (Individuals or Corporations) Have an Interest

The total market value of these securities is estimated at \$112,435,000 of which \$83,644,000 is in stocks and \$28,791,000 in bonds. The bond holdings are principally in two companies, Royal Dutch and Colon Oil Corp. The Colon Oil company, while a domestic corporation, is a subsidiary of the Royal Dutch-Shell group (foreign companies) and has been included as a foreign corporation. Colon Oil is a company incorporated in the United States, owned and operated by a foreign company, all of whose properties are in South America, but whose bonds were sold in the United States (\$10,000,000) at par. These bonds defaulted July 1, 1935, and subsequently the La-Corona Petroleum Maatschappij, a member of the Royal Dutch-Shell group, offered to purchase these debentures at 66% flat. It is not clear why this

[33]

American owned issue, bonds of a Royal Dutch subsidiary, should be in default and that another Royal Dutch subsidiary should offer to buy them at a 33% discount. The Colon Oil Corp. is merely a component of the vast Royal Dutch oil empire. The bonds of the Royal Dutch company are selling far above par, and have always been serviced. It would appear that failure to insist on guarantee by the parent company was expensive to the American investor. The date of incorporation of the company in Delaware was June 26, 1928, the issue date of the bonds July 1, 1928.

Among the larger of our stock holdings in foreign corporations are the publicly owned shares of two of the Standard Oil Co. (N. J.) foreign subsidiaries, namely Imperial Oil, Ltd., and International Petroleum Co., Ltd. Smaller stock holdings are those in Royal Dutch, Shell Transport & Trading, Canadian Oil Companies, Ltd., and others.

In no other field of activity do American companies exercise such a world-wide influence and control as in the oil industry. Exclusive of United States production, the world petroleum production in 1935 amounted to 652,894,000 barrels. Russian production amounted to 178,000,000 barrels. Of the remainder probably 35% is produced by American-controlled companies. Combined with our domestic production and after eliminating the production of foreign companies

[34]

operating in the United States, we find that United States capital controls close to 70% of the world's petroleum production. In 1935 we had an excess of exports, including sales of bunker oil to foreign vessels, of some 80 million barrels of oil (crude and refined), indicating that our large foreign oil investments are not needed to meet any domestic demand, at least not up to the present time. Depletion of our own wells in the future may force us to rely more and more on our foreign oil resources, especially those in South America.

It is difficult to obtain a division of our foreign oil properties between production and marketing facilities. It seems definite, however, that the major portion lies in the latter category. Probably over 80% of our foreign oil production comes from South America and these properties are valued at approximately \$300,000,000. This would include the value of refineries, pipe lines and other equipment necessary to an oil producing unit. In the Far East and Europe nearly all of our investments are in the distribution and marketing divisions.

Mining

Included in this division are investments in those companies whose principal operations consist of the mining and smelting of minerals in foreign countries. Corporations which own mining

[35]

properties but whose activities are primarily in manufacturing, public utility or some other type of industry, are not included. Sufficient data were not available to permit a segregation of their mining properties from other foreign properties.

Investments in foreign copper mines by American copper producers have been held by some economists to have been for the purpose of conserving our own copper resources and to meet existing domestic deficiency due to domestic demand. This does not appear to be borne out by actual condition. For example, in 1935 we imported 481 million pounds of copper, including approximately 27 million pounds of the refined product, and exported 607 million pounds, of which 522 million was refined. Meanwhile, the seven largest United States copper companies operating abroad produced over one billion pounds in 1935, practically all, so far as is known, being refined abroad, at the source of supply. The copper imports into the United States seem to be confined to certain smaller companies operating in contiguous territories, who do their refining in the United States. This would indicate that the greater part of the copper produced by American-owned foreign corporations is sold directly abroad, and that, on balance, we also export whatever foreign copper we import. These figures appear to disprove the belief that the conservation of our domestic resources, to meet our own con-

[36]

sumption needs, has been the motive for our large foreign copper holdings.

American Corporations, All or Substantially All of Whose Assets Are Abroad

The book values of these companies at December 31, 1935, amounted to \$465,592,000 and the market value of their outstanding securities amounted to \$393,035,000.

The largest investment included herein is the Anaconda Mining group whose foreign subsidiaries are the Andes Copper, Chile Copper, Greene Cananea, Silesian American and some other smaller or inactive companies. Their total book value at the end of 1935 was approximately \$300,000,000 and their market value \$240,000,000. No deduction has been made for any assets of these foreign companies located in the United States as the total involved is relatively insignificant. Two-thirds of Anaconda's copper sales are to foreign buyers. The copper supplying these foreign needs comes from Anaconda's foreign mines.

The fact that the market valuation of the above Anaconda subsidiaries is less than the book value, is due mainly to the low price of copper at December 31, 1935. The rising price of copper during 1936 has increased the earning power and hence the value of these investments. As at December 31, 1936, their market values were far in excess of their comparable book values.

[37]

As recited in discussing our foreign oil investments, an important factor affecting the value of our investments abroad is the attitude of foreign governments. In recent years there has been a tendency by foreign governments to increase taxation on foreign-owned properties. The Chilean and Mexican governments are examples of this. Anaconda's foreign subsidiaries are located principally in Chile and Mexico. In Mexico, a law forcing all mining companies to reinvest 25% of their profits within the Republic is being given serious consideration. All such factors affect the value of our foreign holdings and are reflected in the current market price of the shares and bonds.

Among other companies included in this classification are the Cerro de Pasco company, the largest silver producer in the world, Howe Sound, Patino Mines, South American Gold & Platinum, San Toy Mining, Cusi Mexicana, and N. Y. Honduras Rosario. The largest, Cerro de Pasco, has a market valuation considerably in excess of its book value. This is true of practically all of the companies, the only notable exception being the Patino Mines. This latter company, a tin mining enterprise located in Bolivia, has been at a disadvantage because of the lower operating costs of the Malayan tin producers. There is a large foreign interest in the Patino Mines company, but, for purposes of this study, the entire company has been included as American owned, any foreign

interest being considered as part of "foreign investments in the United States." The principal products of these companies are gold, silver, copper, precious stones, and tin. A majority are located in Latin America, a few in Canada, the balance being scattered throughout the Far East and Europe. A portion of the products of certain of these companies is imported into the United States for smelting and refining before resale abroad.

American Corporations Having Wholly-Owned or (51%) Controlled Foreign Subsidiaries

Among the largest United States mining corporations with foreign subsidiaries (exclusive of the Anaconda group discussed heretofore) are the American Smelting & Refining, United States Smelting, Kennecott Copper, Phelps Dodge, American Metals, St. Joseph Lead, and Vanadium Corp. With the exception of American Metals Co., the major part of their assets and operations are in the United States. The products of their foreign properties are to a large extent imported into the United States and sold here. This is especially true of the gold and silver producers. The entire world production of silver in 1935 was 208 million ounces, of which 38 million was produced in the United States. Our imports in that year reached the huge total of 521 million ounces. A survey of all the companies included in this

category indicates that practically all of their silver production was shipped to this country.

The copper production of Matahambre (American Metals) in Cuba is smelted and refined in their Carteret, New Jersey, plant. The Moetzuma Mine in Mexico (Phelps Dodge), inactive due to general operating conditions in Mexico, formerly refined and smelted their product in their Arizona plants.

The total investment of American companies in wholly-owned or (51%) controlled foreign subsidiaries is estimated, at December 31, 1935, at \$190,632,000 book values.

Foreign Corporations Publicly Owned in Which Americans (Individuals or Corporations) Have an Interest

This is the largest type of American mining investment abroad. The market value of this type of holding at December 31, 1935, was \$508,000,000 of which over 50% was in the International Nickel Co. of Canada. Based on data obtained from various sources of reliable information, it is estimated that at December 31, 1935, 40% of the stock of the International Nickel Co. was American-owned.

The great majority of our mining investments in foreign companies are in Canada. In many cases Americans exercise control of the foreign companies. However, it does not always follow

[40]

that control of the directorate means actual majority ownership of the outstanding shares. American bankers have often insisted on control of a company in order to safeguard their interests. American citizens hold the majority of outstanding securities of companies such as Dome Mines, Ltd., Hudson Bay Mining & Smelting, Buffalo Ankerite Gold Mines, Wright-Hargreaves Mines, Ltd., Nipissing Mines, Kerr Lake Mines, Ltd. (main office in New York), and many smaller companies.

Some of the larger American minority holdings in Canadian mining enterprises are found in Hollinger Consol. Mines, Ltd., McIntyre Porcupine Mines, Lake Shore Mines, Ltd., and Teck Hughes, Ltd. Also included in this subdivision are estimates of individual holdings of mining companies which are subsidiaries of American corporations. An example of this is the Premier Gold Mining Co., Ltd., controlled by American Smelting & Refining Co. and also publicly distributed.

Outside of Canada, the chief holdings in this class of investment are in South America, the largest being our bond holdings of Anglo Chilean Nitrate and Lautaro Nitrate.

As stated before, the portfolios of American investment trusts were studied, wherever available, and this examination revealed a surprising list of South African mining company investments not elsewhere published.

[41]

Higher prices prevailing in 1936 for most commodities resulted in higher market prices for outstanding securities of mining companies. Where such prices were available the appreciation in 1936 amounted to \$368,000,000.

Manufacturing and Merchandising

Included in this group are the entire foreign investments of companies whose foreign activities are principally manufacturing. Merchandising investments have also been included, as, in many instances, such investments are merely selling agencies of domestic manufacturers. Foreign investments of canneries, motion picture producers, radio corporations, etc., are included herein. It has been found impractical, from the data available, to attempt the separation of mining investment, woodland holdings, and agricultural property assets from the strictly manufacturing properties of corporations whose main activities are manufacturing.

American Corporations Having Wholly-Owned or (51%) Controlled Foreign Subsidiaries

The bulk of our foreign investments in manufacturing is in American-owned and controlled subsidiaries. The book value of these investments is estimated, at December 31, 1935, at \$1,239,392,000. No market values were available.

[42]

In arriving at this estimate, the records of over a thousand manufacturing corporations were studied. This number refers only to parent companies. If subsidiaries were counted the resulting total would be several times as large; for example some twenty of our large manufacturing systems alone have over a thousand foreign subsidiaries.

Book valuations were used exclusively as a basis of valuation. In many cases individual subsidiary balance sheets were not available and perhaps the value as expressed in the parent company balance sheet may have been too high or too low. Where companies were listed on a stock exchange the registration statements filed therewith revealed many such incorrect valuations and adjustments were made accordingly. The most frequent cause of difference was due to the practice of certain parent corporations not including any surplus accumulated abroad since purchase or formation of the subsidiary.

There are certain adverse factors affecting many of these investments which are not reflected in book valuations. For example, properties domiciled in Germany have a rather doubtful value today. Some of the large investments in Germany are those of the International Harvester, General Electric, General Motors, National Cash Register, Eastman Kodak, Libby Owens Ford, E. G. Budd, Remington Rand, Woolworth, Addressograph Multigraph, and American

[43]

Radiator. They probably comprise over 50% of all our German manufacturing establishments.

Doubtful values can also be ascribed to our investments in certain other European and South American countries where the governments of these countries have practically nationalized foreign investments.

Foreign Corporations Publicly Owned in Which Americans (Individuals or Corporations) Have an Interest

Our holdings of stocks of foreign manufacturing and merchandising corporations are estimated, at December 31, 1935, at \$436,571,000 market values, and the bonds of foreign corporations at \$99,455,000 market values. The bonds have a face value of \$266,312,000.

The large investment in stocks is due principally to the holdings of Woolworth, Ltd., by the F. W. Woolworth Co. At market these shares were worth, at December 31, 1935, \$228,106,977. While these holdings are in the nature of a controlling interest (over 51%) the shares of the English subsidiary are publicly owned and widely held both by Americans and Englishmen. This investment (at market values) constitutes our greatest single foreign corporate stock ownership.

Other large stock holdings are those in Electrical & Musical Industries, Ltd., Distillers Seagrams, Ltd., Hiram Walker G. W., Aluminum,

Ltd., Imperial Tobacco (Canada), Imperial Tobacco (Ltd.), Singer, Ltd., Ford Motor, Ltd. (England), Ford Motor of Canada, Ltd., Swift International (considered as all American-owned), and British American Tobacco Co., Ltd. Securities of these companies are traded on American stock exchanges and have been publicly offered in this country.

In the bond section, we find the much discussed International Match and Kreuger & Toll holdings of American investors as the largest included. Approximately \$150,000,000 was invested in these two bond issues and, at December 31, 1935, their market value was approximately \$22,000,000. Also included are many German issues floated in this country that are now selling at approximately 20 cents on the dollar and have been in default for a number of years. Canadian and a few Italian corporate issues constitute the larger part of the remainder.

The market value of our holdings of stocks and bonds in foreign manufacturing and merchandising corporations increased from approximately \$536,000,000 at December 31, 1935, to \$706,000,000 at December 31, 1936.

Miscellaneous

Included herein are all those foreign investments which did not fit into any of the other fields

of industry. Banks, fire and casualty insurance companies, construction companies, hotels, air transportation, real estate companies, some miscellaneous investment trusts whose foreign securities were not identifiable as to industrial allocation, and newspapers are some of the types of commercial enterprises comprising the total of our miscellaneous investments abroad. In all, they are estimated, at December 31, 1935, at book value of \$199,627,000, and market value of \$145,125,000.

American Corporations, All or Substantially All of Whose Assets Are Abroad

These amount to approximately \$26,488,000 book value, and \$11,142,000 market value. A number of Cuban enterprises, principally National Hotels of Cuba and Havana Docks, and two investment trusts whose holdings consist principally of German internal mortgages, the German Credit & Investment Corp. and the International Mortgage & Investment Corp., are included herein.

American Corporations Having Wholly-Owned or (51%) Controlled Foreign Subsidiaries

The total book value of foreign investments of these companies, at December 31, 1935, was estimated at \$98,682,000, no market value available. They consist principally of the net invested capi-

tal of the foreign branches of American banks, notably Chase, National City, and Guaranty Trust, the controlling interest of the Transamerica Corp. in the Banca D'America and Italia, the net interest of American insurance companies (excluding life insurance) and other miscellaneous investments such as the holdings of American Express, Ford Hotels, Commercial Investment Trust, Commercial Credit Co., Pan American Airways, and New York *Herald Tribune*.

Foreign Corporations Publicly Owned in Which Americans (Individuals or Corporations) Have an Interest

The market value of American-owned stocks at December 31, 1935, was estimated at \$9,607,000 and bonds at approximately \$25,694,000. The face value of the bonds was \$64,850,000. The stock holdings consist for the most part of foreign shares held by American investment trusts.

In the bond section are a large number of German banks and miscellaneous organizations which account for the comparatively low market value. They include German Central Bank of Agriculture, Ruhr Housing, Commerz & Privat Bank, Deutsch Bank, Protestant Church of Germany, Roman Catholic Welfare Institutions, Leipzig Trade Fair, etc. They all sell at about 20 cents on the dollar. A number of Canadian buildings that have had their bonds sold in the United

States are next in size and are also selling at considerable discounts from their issue price. Admiral Beatty Hotel, Vancouver Georgia Hotel, Pacific Coast Terminals, Montreal Insurance Exchange are a few. About ten Hungarian banks and credit institutions, including the Hungarian Discount & Exchange Bank, Hungarian Land & Mortgage Institution, Hungarian Italian Land Bank, etc., are also showing a large depreciation in market price. Practically all of the institutions mentioned are in complete default as to interest.

Foreign Government and Government-Guaranteed Bonds

Approximately \$9,000,000,000 (face amount) of foreign government and government-guaranteed issues were publicly offered in the United States in the years 1914-1931. Practically all bond issues floated before 1914 have been either redeemed or refunded, or are valueless due to complete default. Of this sum total of \$9,000,000,000 only \$4,596,000,000 are still outstanding in their original form—as dollar bonds—and of this amount, we estimate that, at December 31, 1935, approximately \$1,415,000,000 were in the hands of foreigners and \$3,180,637,000 held by Americans. The market value of these bonds, still held by Americans, at December 31, 1935, was \$2,342,228,000.

[48]

The decline in total dollar bonds outstanding has been due to both normal and abnormal activities. Reductions would normally occur through redemptions and sinking fund activities, as contracted. These operations account for a considerable part of the reduction. In addition, however, many sinking funds have taken advantage of favorable market conditions prevailing during recent years and have purchased in the open market, at substantial discounts, large blocks of bonds which were then retired. A great many bonds were thus purchased during the years 1932 to 1935 inclusive, a period of wholesale defaults and low market prices. We find here the curious anomaly of debtors pleading lack of dollar exchange as the reason for their interest default, but at the same time using their dollar balances to repurchase these same defaulted bonds at bargain prices. During the four years 1932 to 1935 approximately \$412,000,000 (face value) of foreign dollar bonds were presented for cancellation. These bonds were probably bought at prices averaging less than half of their face value and represented losses of hundreds of millions of dollars to American investors.

Another item tending to lessen the outstanding amount of dollar bonds has been the practice of converting dollar bonds into internal currency issues. This is done where sizeable amounts of dollar bonds have been repatriated by foreigners

[49]

(individuals or governments). These bonds are not presented for cancellation to the United States trustees of the dollar bond issues, but held by the foreign governments as collateral against the internal currency bonds issued. This practice results in a distorted figure of outstanding dollar bonds and we have deducted such items from the outstanding amount wherever the information was obtainable. Examples of this type of operation are:

	Outstanding 12/31/36 per Trustees Books	Converted Into Internal Loans	Actually Outstand- ing at 12/31/36
Vienna 6s/1932	\$24,035,500	\$21,774,500	\$2,261,000
Lower Austria 7½/1930 ..	1,578,500	1,131,500	447,000
Styria 7s/1946	2,731,500	2,602,500	129,000
Graz 8s/1934	2,144,700	1,620,000	524,700
Tyrol Hydro Electric 7½/1935	2,503,000	255,000	2,248,000
Tyrol Hydro Electric 7s/1932	2,241,000	256,000	1,985,000
	<u>\$35,234,200</u>	<u>\$27,639,500</u>	<u>\$7,594,700</u>

In other words, on these six issues alone the outstanding amounts of bonds as shown by trustees books are overstated to the amount of \$27,639,500. We have deducted all such holdings from the amount of Dollar Bonds outstanding in arriving at our figure of \$4,596,000,000.

As stated heretofore, we estimate that, at December 31, 1935, the face amount of foreign bonds outstanding held by Americans amounted to \$3,180,637,000 and the amount held by foreigners

\$1,415,000,000. The Department of Commerce estimated foreign holdings of "Portfolio" investments (includes foreign corporation issues publicly offered in the United States) at \$1,100,000,000. As explained earlier in this report, we believe that part of the difference in the two estimates lies in the fact that we have excluded from American holdings, Canadian investments of American life insurance companies held by the Canadian government as collateral against actuarial liability of those companies to Canadian policyholders.

In the course of our research we have found various interesting examples of repatriations. Many of these operations were of necessity conducted under a cloak of secrecy and to lift this veil and let in the light is, in most cases, extremely difficult. Many times it is only after the redemption or refunding of an issue takes place that the small American holdings are disclosed. This is illustrated in the case of Province of Upper Austria bonds—7s/1945 and 6½/1937 called for redemption in December, 1935. At time of redemption there were \$10,149,000 bonds outstanding, but as was disclosed to us, all but approximately \$400,000 bonds were held by the issuer. In their Balance of International Payments, 1935, the U. S. Dept. of Commerce included as "Bond redemption payments received" the sum of \$9,129,000 as paid by Austria. This naturally has

resulted in an overstatement of "receipts from bond redemptions" for 1935, and, following through, will effect a distortion of other items in the Balance of International Payments compilation. These two bond issues were originally issued here in 1925 and 1927.

While repatriations and repurchases have taken place in all foreign government bonds, it should be pointed out that some of these operations were entirely legitimate and within the bounds of international financial honesty. The deciding factor, of course, is the status of the interest payments when such purchases are made. If the interest is being serviced in full and all covenants of the bond indenture are being met, a foreign debtor is clearly entitled to pick up any bargains existing in his own obligations. Financial panics in creditor countries (especially in the United States) can be and have been used by foreign nations and their citizens to pick up their own external bonds at bargain prices. Japan, Australia, France, Holland, Canada, Belgium, and Sweden have considerably and profitably lightened their external debt payments to the United States through the medium of repurchases during times of financial stress in the United States. In contrast to England, where foreign lending is practiced more scientifically, our foreign loans are bought by the investing public in small amounts, the average purchase being around \$3,000. When financial

[52]

stringencies occur, such as happened in 1929 to 1935, many holders are forced to sell and others, not having the knowledge and experience necessary to evaluate correctly the worth of their foreign bond holdings, are easily frightened and throw them overboard at sacrifice prices. The situation in England differs considerably from ours. Foreign loans are usually held in large blocks by the various banks, investment houses and trusts, who are better equipped to hold on to the bonds and to deal collectively with defaulting foreign governments. An institution known as the "Council of Foreign Bondholders" deals with all situations of this kind. Foreign debtors cannot default and then buy up their defaulted bonds at bargain prices. The bonds are simply not for sale.

Another factor tending to reduce the amount of foreign bonds in American hands is the purchase by nationals of a third nation of foreign bonds held by United States citizens. During the years 1930, 1931, 1932 large quantities of Argentine dollar bonds were purchased by English investors, at very low prices. It is generally estimated that 50% of our Argentine dollar bond holdings were so acquired by the English.

In summary, out of a total of \$9,000,000,000 of foreign government and government-guaranteed bonds issued and sold to American investors, we now hold bonds, at face value, of \$3,180,637,000

[53]

market value of \$2,342,228,000. The amount of dollars received by American investors for the \$6,000,000,000 (approximate) of bonds surrendered and the amount of loss sustained upon their surrender are unknown. No estimate with respect thereto has ever been made by the government.

Geographical Division of Foreign Investments

The division of investments by territory as set forth on Exhibit "C" can only be considered as approximate. American citizens have investments in Canadian, English and other foreign corporations whose activities are worldwide. The location of these investments has been determined by the country in which incorporated. American companies, while furnishing data as to the total amount invested abroad and the foreign countries in which they operate, seldom divide their investment by countries.

The following is a condensed summary of investments divided geographically:

Investments by Territories at December 31, 1935

		Percentage of total
Canada and Newfoundland	\$3,043,252,000	37%
Europe	2,017,229,000	25%
Latin America	2,146,201,000	26%
Africa, Asia and Oceania	1,021,600,000	12%
Total	<u>\$8,228,282,000</u>	

[54]

Following is a comparison of our long-term debtor-creditor position at December 31, 1935, by geographical division, subject to the above qualification and the qualification stated by the Department of Commerce with respect to its division, to wit:

"It is important to note that the geographical distribution of foreign holdings of United States investments . . . does not necessarily reflect the true ultimate ownership."

	Our Long-Term Investments Abroad As at Dec. 31, 1935	Foreign Long-Term Investments in United States* As at Dec. 31, 1935
Canada and Newfoundland	\$3,043,252,000	\$1,000,000,000
Europe	2,017,229,000	3,491,000,000
Latin America	2,146,201,000	43,000,000
Africa, Asia and Oceania	1,021,600,000	495,000,000
Total	<u>\$8,228,282,000</u>	<u>\$5,035,000,000</u>

As set forth above, at December 31, 1935, we were a debtor with Europe on long-term account, exclusive of war debts, in the amount of \$1,474,000,000. This debtor position has been increased during the past year. Report of the Treasury Department reveals purchases by Europeans of foreign and American securities between December 31, 1935, and September 30, 1936, in the amount of \$356,000,000. Further, appreciation in market value of European investments in American securities exceeded the appreciation in market values of our investments in Europe.

* Department of Commerce estimate.

[55]

This net gain to Europe, at September 30, 1936, we estimated at approximately \$200,000,000, leaving our net long-term debtor position with Europe, at September 30, 1936, at approximately two billion dollars—exclusive of war debts.

Problem of Transfer of Earnings and Effect of American Investments Abroad on Import and Export Statistics

It is interesting to observe the amount of our investments abroad as to which we need have no transfer difficulties in the payments to security holders of interest and dividends, due to the fact that these companies accumulate dollar balances in the United States through the sale of their products imported into this country. The total of such investments are estimated at approximately three billion dollars, representing principally investments in certain mining, oil, agricultural, paper and pulp, and rubber companies.

Of all our foreign investments, it would appear that there are only two groups, as a whole, which do not tie in with our domestic economy—our investment in bonds of foreign governments and our public utility investments. Our greatest losses have been in securities of these groups—in enterprises which do not serve either as feeders of imports or outlets for exports.

Where American corporations producing abroad sell part or all of their products in this country,

their outstanding securities can be serviced out of dollar balances created here through sale of goods. With respect to our railroad investments abroad, those roads running through Canada, Mexico, Central America, and Cuba handle freight shipped by American corporations, payment for which, except where foreign legislation forbids, could be made in the United States, and outstanding securities serviced out of those dollar balances.

There has been set forth heretofore the extent of the dependence of our sugar investments in Cuba on the market for Cuban sugar in this country. The same is true of paper and pulp and rubber investments. Other investments—in oil and mining—enter into our domestic affairs through import, refining and re-export. Some of our foreign manufacturers—though proportionately few—sell their foreign manufactured product in the American market. Many of our foreign railroad investments are branch lines of American systems, such investments being made for economy of operation. Other foreign railroad investments are supported by American-owned companies engaged in producing goods for the American market. Our investments in resort hotels in Cuba and Canada depend principally on the American tourist trade.

With respect to our import statistics, it will be noted that where goods are exported from a

foreign country to this country by an American-owned foreign corporation, the value stated in our import statistics may not be equivalent to the amount remitted abroad by the parent company in America. The latter company will be guided in its remittances abroad primarily by the requirements of the foreign subsidiaries, which remittances may be more or less than the stated import valuation. An investigation made in England in recent years showed, for example, that only 40% of the actual export value of rubber from British-owned Malayan rubber plantations was actually remitted to Malaya, the balance being retained in London for head office expenses, taxes and dividends.

Likewise, considerable of our exports are shipped to selling agencies abroad, which, in remitting to the home office, will deduct from the amounts actually realized commissions, foreign taxes and sundry expenses. Consideration must also be given to the fact that, as in domestic business, many sales will never be paid for and eventually will be charged off to bad debts. Furthermore, slow moving merchandise may be disposed of at prices considerably less than the value at the time of export.

The reported earnings of our foreign subsidiaries, it can readily be seen, are subject to the accounting procedure of the parent company in America. Foreign subsidiaries producing for the

[58]

American market may show no profits, the parent company in effect taking up the profit through low cost of its imports. Similarly, selling agencies abroad, though profitable to the parent company in providing a sales outlet, may maintain accounts in such a manner as to show only selling and other expenses, the profits on sales being taken up by the parent company in its selling price to the foreign subsidiary.

Respectfully submitted,

(signed)



Certified Public Accountants

American Long-Term Investments Abroad as at December 31, 1935

(In Thousands of Dollars)

	American corporations, all or substantially all of whose assets are abroad		American corporations having wholly-owned or (51%) controlled foreign subsidiaries		Foreign corporations publicly owned in which Americans (individuals or corporations) have an interest			Foreign government, provincial, municipal and government-guaranteed issues		TOTAL	
	Book Value	Market Value	Book Value	Market Value	Stocks		Bonds		* Book Value	† Market Value	
					Market Value	Face Value	Market Value	Face Value			
Foreign Government, Provincial, Municipal and Government-guaranteed issues	—	—	—	—	—	—	—	3,180,637	2,342,228	3,180,637	2,342,228
Railroads	187,772	52,416	82,294	38,045	158,077	139,813	—	—	—	466,188	312,568
Public Utilities ...	862,860	359,780	142,426	86,028	426,972	341,264	—	—	—	1,518,286	929,498
Agriculture, including Rubber ...	270,531	66,269	203,348	3,244	524	510	—	—	—	477,647	273,371
Paper and Pulp ..	130,653	57,101	110,391	3,156	69,972	36,774	—	—	—	314,172	207,422
Oils	120,544	51,992	986,557	83,644	29,485	28,791	—	—	—	1,230,240	1,150,984
Mining	465,592	393,035	190,632	489,459	50,930	18,542	—	—	—	1,196,613	1,091,668
Manufacturing and Merchandising .	—	—	1,239,392	436,571	266,312	99,455	—	—	—	1,942,275	1,775,418
Miscellaneous	26,488	11,142	98,682	9,607	64,850	25,694	—	—	—	199,627	145,125
	2,064,440	991,735	3,053,722	1,149,754	1,067,132	690,843	3,180,637	2,342,228	10,515,685	8,228,282	

* Includes foreign stocks at market values, as cost to Americans is unobtainable.

† Includes investments of American corporations in wholly-owned or (51%) controlled foreign subsidiaries at book values as no market values for these investments are obtainable.

EXHIBIT "B"—Schedule 1

AMERICAN LONG-TERM INVESTMENTS ABROAD

Governments

Foreign Governments, Provincial, Municipal and Government-Guaranteed Issues

AS AT DECEMBER 31, 1935

(In Thousands of Dollars)

	Face Value	Market Value
Canada	951,062	1,008,784
Europe	866,385	594,818
Latin America	953,976	341,229
Asia, Africa and Oceania	409,214	397,997
	3,180,637	2,342,228

EXHIBIT "B"—Schedule 2

AMERICAN LONG-TERM INVESTMENTS ABROAD

Railroads

AS AT DECEMBER 31, 1935

(In Thousands of Dollars)

[62]

	American corporations, all or substantially all of whose assets are abroad		American corporations having wholly- owned or (51%) controlled foreign subsidiaries	Foreign corporations publicly owned in which Americans (individuals or corporations) have an interest		
	Book Value	Market Value	Book Value Only	Stocks		Bonds
				Market Value Only	Face Value	Market Value
Canada	—	—	43,226	36,150	120,256	115,998
Europe	—	—	—	1,895	18,958	15,385
Latin America	183,706	51,219	39,068	—	18,863	8,430
Asia, Africa and Oceania	4,066	1,197	—	—	—	—
	187,772	52,416	82,294	38,045	158,077	139,813

EXHIBIT "B"—Schedule 3

AMERICAN LONG-TERM INVESTMENTS ABROAD

Public Utilities

AS AT DECEMBER 31, 1935

(In Thousands of Dollars)

[63]

	American corporations, all or substantially all of whose assets are abroad		American corporations having wholly- owned or (51%) controlled foreign subsidiaries	Foreign corporations publicly owned in which Americans (individuals or corporations) have an interest		
	Book Value	Market Value	Book Value Only	Stocks		Bonds
				Market Value Only	Face Value	Market Value
Canada	5,772	3,206	75,261	41,809	225,315	218,006
Europe	124,129	63,164	25,200	41,344	140,342	72,080
Latin America	626,161	250,327	4,730	2,875	3,300	2,900
Asia, Africa and Oceania	106,798	43,083	37,235	—	58,015	48,278
	862,860	359,780	142,426	86,028	426,972	341,264

AMERICAN LONG-TERM INVESTMENTS ABROAD

Agriculture

(Including Rubber Plantations)

AS AT DECEMBER 31, 1935

(In Thousands of Dollars)

[79]

	American corporations, all or substantially all of whose assets are abroad		American corporations having wholly- owned or (51%) controlled foreign subsidiaries	Foreign corporations publicly owned in which Americans (individuals or corporations) have an interest		
	Book Value	Market Value	Book Value Only	Stocks		Bonds
				Market Value Only	Face Value	Market Value
Canada	—	—	23,731	3,244	524	510
Europe	—	—	—	—	—	—
Latin America	260,451	56,118	141,472	—	—	—
Asia, Africa and Oceania	10,080	10,151	38,145	—	—	—
	270,531	66,269	203,348	3,244	524	510

AMERICAN LONG-TERM INVESTMENTS ABROAD

Paper and Pulp

AS AT DECEMBER 31, 1935

(In Thousands of Dollars)

[65]

	American corporations, all or substantially all of whose assets are abroad		American corporations having wholly- owned or (51%) controlled foreign subsidiaries	Foreign corporations publicly owned in which Americans (individuals or corporations) have an interest		
	Book Value	Market Value	Book Value Only	Stocks		Bonds
				Market Value Only	Face Value	Market Value
Canada	128,431	54,879	110,391	3,156	69,972	36,774
Europe	—	—	—	—	—	—
Latin America	—	—	—	—	—	—
Asia, Africa and Oceania	2,222	2,222	—	—	—	—
	130,653	57,101	110,391	3,156	69,972	36,774

EXHIBIT "B"—Schedule 6

AMERICAN LONG-TERM INVESTMENTS ABROAD

Oils

AS AT DECEMBER 31, 1935

(In Thousands of Dollars)

	American corporations, all or substan- tially all of whose assets are abroad		American corporations having wholly- owned or (51%) controlled foreign subsidiaries	Foreign corporations publicly owned in which Americans (individuals or corporations) have an interest		
	Book Value	Market Value	Book Value Only	Stocks	Bonds	
				Market Value Only	Face Value	Market Value
Canada	—	—	122,966	76,496	420	437
Europe	2,010	524	225,845	6,598	19,075	21,554
Latin America	118,534	51,468	392,569	550	10,000	6,800
Asia, Africa and Oceania	—	—	245,177	—	—	—
	120,544	51,992	986,557	83,644	29,495	28,791

[99]

EXHIBIT "B"—Schedule 7

AMERICAN LONG-TERM INVESTMENTS ABROAD

Mining

AS AT DECEMBER 31, 1935

(In Thousands of Dollars)

	American corporations, all or substan- tially all of whose assets are abroad		American corporations having wholly- owned or (51%) controlled foreign subsidiaries	Foreign corporations publicly owned in which Americans (individuals or corporations) have an interest		
	Book Value	Market Value	Book Value Only	Stocks	Bonds	
				Market Value Only	Face Value	Market Value
Canada	28,938	30,421	12,296	451,696	—	—
Europe	9,470	5,587	—	—	1,793	605
Latin America	421,513	349,479	164,622	1,710	49,137	17,937
Asia, Africa and Oceania	5,671	7,548	13,714	36,053	—	—
	465,592	393,035	190,632	489,459	50,930	18,542

[67]

EXHIBIT "B"—Schedule 8

AMERICAN LONG-TERM INVESTMENTS ABROAD

Manufacturing

As At December 31, 1935

(In Thousands of Dollars)

[89]

	American corporations, all or substan- tially all of whose assets are abroad	American corporations having wholly- owned or (51%) controlled foreign subsidiaries	Foreign corporations publicly owned in which Americans (individuals or corporations) have an interest			
					Bonds	
			Book Value	Market Value	Stocks Market Value Only	Face Value
Canada	Too small to treat separately, included under caption "Ameri- can corps. having wholly-owned or (51%) controlled foreign subsidiar- ies"	425,150		95,852	30,733	27,710
Europe		498,142		289,204	235,579	71,745
Latin America		187,200		51,515	—	—
Asia, Africa and Oceania		128,900		—	—	—
		1,239,392		436,571	266,312	99,455

EXHIBIT "B"—Schedule 9

AMERICAN LONG-TERM INVESTMENTS ABROAD

Miscellaneous

As At December 31, 1935

(In Thousands of Dollars)

[69]

	American corporations, all or substan- tially all of whose assets are abroad	American corporations having wholly- owned or (51%) controlled foreign subsidiaries	Foreign corporations publicly owned in which Americans (individuals or corporations) have an interest			
					Bonds	
			Book Value	Market Value	Stocks Market Value Only	Face Value
Canada	—	18,430	2,683	7,796	3,990	
Europe	3,187	52,820	6,427	57,054	21,704	
Latin America	23,301	15,832	197	—	—	
Asia, Africa and Oceania	—	11,600	300	—	—	
	26,488	98,682	9,607	64,850	25,694	

American Long-Term Investments Abroad—Distributed Geographically—
as at December 31, 1935

(In Thousands of Dollars)

	CANADA		EUROPE		LATIN AMERICA		ASIA, AFRICA, AND OCEANIA		TOTAL	
	* Book Value	† Market Value	* Book Value	† Market Value	* Book Value	† Market Value	* Book Value	† Market Value	* Book Value	† Market Value
Foreign Government, Provincial, Municipal and Govern- ment-guaranteed issues	951,062	1,008,784	866,385	594,218	953,976	341,229	409,214	397,997	3,180,637	2,342,228
Railroads	199,632	195,374	20,853	17,280	241,637	98,717	4,066	1,197	466,188	312,568
Public Utilities	348,157	338,282	331,015	201,788	637,066	260,832	202,048	128,596	1,518,286	929,498
Agriculture, including										
Rubber	27,499	27,485	—	—	401,923	197,590	48,225	48,296	477,647	273,371
Paper and Pulp	311,950	205,200	—	—	—	—	2,222	2,222	314,172	207,422
Oils	199,882	199,899	253,528	254,521	521,653	451,387	245,177	245,177	1,220,240	1,150,984
Mining	492,930	494,413	11,263	6,192	636,982	533,748	55,438	57,315	1,196,613	1,091,668
Manufacturing and Merchandising ..	551,735	548,712	1,022,925	859,091	238,715	238,715	128,900	128,900	1,942,275	1,775,418
Miscellaneous	28,909	25,103	119,488	84,139	39,330	23,983	11,900	11,900	199,627	145,125
	3,111,756	3,043,252	2,625,457	2,017,229	3,671,282	2,146,201	1,107,190	1,021,600	10,515,685	8,228,282

* Except as to foreign stocks which in all cases are valued at market, as original cost to Americans is unobtainable.
† Includes investments of American corporations in wholly-owned or 51% controlled foreign subsidiaries at book values as no market values for these investments are obtainable.

“Aid slighted truth, with thy persuasive strain
Teach erring man to spurn the rage of gain;
Teach him that states of native strength possess,
Tho’ very poor, may still be very blest;
That trade’s proud empire hastes to swift decay,
As ocean sweeps the labour’d mole away;
*While self dependent power can time defy,
As rocks resist the billows and the sky.*”

Goldsmith—“*The Deserted Village.*”

February 25, 1937.

My dear Mr. President:

Herewith I am sending for your attention a memorandum which deals with the plan for increasing the withholding rate of tax on income received by non-resident aliens and foreign corporations. This was prepared in accordance with your request that the matter be given further study.

Faithfully yours,

The President,

The White House.

Enclosure.

MEMORANDUM FOR THE PRESIDENT:

At a conference on February 17, there was submitted to you a plan for increasing the withholding rate of tax on income received by non-resident aliens and foreign corporations. You suggested further study of this plan with a view to avoiding an increase in the rate of tax on income from long-term investments. This further study has been made and the conclusion is that the plan, modified in this fashion, cannot be made administratively feasible because, unlike a transfer tax, it would require the determination of the identity of the foreigner, the nature of his interest and the length of time he had held the securities in question. These facts could not be satisfactorily determined for the following reasons:

1. In the case of stock, the records of its ownership in the United States are not sufficient because a considerable amount of stock has been held abroad for many years in the name of banks, brokers, or other fiduciaries, with no reliable records in this country and available to the Treasury indicating the actual owners of such stock.

The great mass of bonds are unregistered bearer bonds and debtor corporations in this country have no records of the actual owner of such bonds other than the name disclosed on ownership certificates presented at the time of interest payments. These certificates cannot be wholly relied upon because transfers

of ownership can take place without any corresponding change in these certificates of ownership.

2. The Bureau could not depend upon statements of identity, interest and period of ownership made by foreign investors because of the danger of their being self-serving. The Bureau would be unable to verify such statements by actual inspection of the foreign investor's records, and the Government would have no control over the person of a foreign investor enabling it to set up penalties effective to prevent the making of false statements.

3. In the absence of reliable records as pointed out above, it would not be feasible to adopt arbitrary rules as to ownership, such as a rule treating record ownership as actual ownership, or arbitrary rules as to period of ownership. Such arbitrary rules would have to be made so narrow in the process of preventing evasion that they would give relief to only a small class of long-term investors.

In the case of stock, to accept record ownership as actual ownership would place a premium on stock held abroad for a period of years especially by banks or brokers because foreign investors would seek to acquire stock so held without transferring record ownership since dividends on such stock would escape the higher tax rates. It would create in many cases two prices for the same security. Again, a rule that ownership remains unchanged until record ownership is changed would permit and encourage dealing in stocks held by banks and brokers.

4. Finally, any plan imposing two widely divergent rates of tax operating simultaneously would create serious administrative difficulties if the lower rate of tax was to be confined in actual operation to the class of foreign investors entitled thereto.

(a) The attempt to apply different rates of withholding at the source would impose upon withholding agents the additional burdensome obligation of ascertaining the facts necessary to determine in the case of each interest or dividend payment the proper rate of withholding.

(b) To require withholding at the maximum rates in all cases and adjustment thereafter by the Commissioner would entail a severe administrative burden upon the Bureau of Internal Revenue and require additional appropriations to make such refunds. In such cases also the Bureau would be confronted with the problem of securing adequate proof of the foreigner's identity, his actual interest in the securities in question and the length of time he had held them.

Note: The great mass of the foregoing difficulties would not be present in the case of a transfer tax because, in the latter case, it would be necessary to determine merely one fact, *viz.*, that a particular transaction involved a foreigner. His identity would not have to be determined, the character of his interest would not have to be ascertained, and the length of time he had held his securities would not have to be considered.

February 25, 1937.

MEETING ON FRENCH SITUATION

February 26, 1937
9:15 A.M.

Present: Mrs Klotz
Mr. Taylor/
Mr. Lochhead/
Mr. White,
Mr. Knoke,

H.M.Jr: Now, I tell you what I want. I've come to the conclusion that this French thing is just about as bad as it can be, see? Can't be any worse. And if the French fail, why, there goes our tripartite agreement. And what are we going to do? See?

I think that the French, talking in the room here, have been kidded a little bit in thinking that they may get a loan.

Knoke: Here?

H.M.Jr: Yes. We've got to talk very confidentially. I think that Bullitt's cables and what Bullitt tells them don't check. I mean I've got to talk very confidentially. And I think their hopes have been sort of raised, that he's led Blum to believe that if he makes some sort of gesture on the debts, he can float a loan here. Well, that's perfectly asinine, and I think Bullitt - I mean Blum just doesn't realize.

And then the two cables came in that he wants - Tripp told Cochran that the Dutch turned them down flat on a five billion franc loan. And Bullitt told Blum that if they made a gesture on this debt business, they might get a loan here. And then Cochran sort of saw the papers afterwards and said there was no such thing, wouldn't give the French any kind of loan. Everybody talking about the loan and all that kind of stuff.

Well, the only thing that the French can do to save themselves would be an additional devaluation, see, going the other eight percent, which would give them seven hundred million.

- 2 -

Taylor: Seven billion.

White: Little more than seven billion francs.

Taylor: Last three months.

White: Taking it out of the stabilization fund. Not really a profit. But they're talking about using that.

H.M.Jr: Well, I talked to Cochran for thirty minutes, and just get this - I mean I've played my hunches and then I get all the facts I can about it. Let's see, of thirty million pounds sterling which they got from England - well, they got it in three installments; there's one installment yet to come - it's all gone but a million and a half. Just get that; it's all gone.

Knoke: You say the thirty million?

H.M.Jr: Of the thirty million....

Knoke: But that was forty.

H.M.Jr: That would be thirty million so far paid. Everything is gone but a million and a half.

Knoke: Yes.

H.M.Jr: So with the other ten million to come, at the rate it's going, they can last another ten days and then they're through. See? I mean that's worth coming down to Washington for, isn't it?

Knoke: Yes.

H.M.Jr: I mean I like to bring you down for good news, but I didn't even know it was as bad as that.

Now, I talked to the President last night about seven-thirty and gave him - for the first time I said, "Mr. President, I've got a new idea, a new hunch. I think we've got to tell the French that the only way they can save themselves is through devaluing the limit." And he's interested and I'm to go over and see him this morning at 10:10, see? He's delaying his press conference in order to see

- 3 -

me.

But again, I have my hunches and then I get my information. I spoke to Cochran and Cochran was very, very urgent in his request that I wait until tonight, because Blum and Flandin are going to have a debate this afternoon, and he said out of that may come something. So Cochran says we've got nothing to gain by moving this morning and everything to gain - we have nothing to lose by - no, nothing to gain by moving this morning, everything to lose, and he strongly urged me to wait until he could get a summary of the debate.

And then, he's made a very intensive study of the situation as to what can be done. That is, if we suggested this morning to the French that they devalue, it might just fall on hard ground, and they are not ready; but they might be ready Monday. But he says certainly this debate this afternoon between Blum and Flandin is going to be of terrific importance. We'll have a man present and he'll listen and they'll get it off tonight.

But he says the trouble is that Blum insists on keeping the present people at the head of the Bank of France and they are technically unfit to administer it. So I said, "Well, how about Rist as the head of the Bank?" He said it would be marvelous; he said he's equipped and all that. But he says that they have to have a change in personnel in order to gain the confidence there. He said just devaluation and a loan won't do the thing, but they'll have to have a change in personnel in the Bank of France and possibly the Treasury - but certainly the Bank of France.

And now, that gives you a view of the political situation. Now, I asked White to work through the night for me and tell me what - could we stand this.

White:

It would affect us very little, so small - I'm speaking of France alone now, with the assumption that sterling will remain as it is. But France alone is so small that it is not a factor in your considerations. The other factors are far more important.

- 4 -

- Lochhead: What about Switzerland and Holland?
- White: I'm assuming that they don't change. The Netherlands wouldn't; Switzerland might.
- Knoke: To what extent would devaluation to the lower level of four thirty-five in terms of the dollar affect the tripartite agreement?
- H.M.Jr: Well, as I understand it, they can do that within the tripartite agreement.
- Lochhead: Yes, within the tripartite agreement.
- Knoke: That was my feeling, but that's been questioned time and again.
- Lochhead: Well, the only question is outside, isn't it?
- Knoke: That's right.
- Taylor: I don't think there's any question about that.
- H.M.Jr: My interpretation is they passed this law saying that they could, and as I remember the thing - somebody refresh my memory - they said they would go from such and such a point to - from 24 point.... what was it?
- Lochhead: From 24 to 34.5.
- H.M.Jr: Yes
- Lochhead: And they mentioned that they were - they mentioned at the beginning they were going to start at the middle. We thought they would vary. We never thought they were going to peg it at the middle rate. When the thing started out, I don't think anybody thought they were going to try to hold it right at the middle rate. Then they did start and the people took it for granted that the middle rate was to stick.
- H.M.Jr: That's what I asked Knoke to come down for. I want every brain on this I can get.

- 5 -

- Knoke: I have another question. Do we know how the British would feel about it?
- White: According to the tripartite agreement arrangement, the British shouldn't take any more action than we should, because their understanding was based on the French statement of 25.2 to 34.3.
- H.M.Jr: I was going to send for the British today, but in view of what Cochran says, I think... As I get it, Blum has this debate this afternoon and Blum is scheduled for another one of those Sunday speeches. By Monday morning we'll get the reaction to what happens today plus his Sunday speech, and I think it's time enough to talk to the British Monday. No use talking to them today; they're all on their week-ends.
- Taylor: Monday's plenty of time, better.
- H.M.Jr: I have changed. When I sent for you last night I thought I was going to do more today, but with all this going on I think we better wait and see - my second thought - what happens this evening, what Blum says Sunday, and then digest it; have a meeting Monday and then get this thing, make up our mind Monday.
- White: Moreover, I don't think there's any doubt in the French mind that we will agree. We couldn't do other than agree. So that any such statement on our part now will not aid them much, because they already expect that. Unless you contemplate doing beyond that as an assistance, it's another reason why there is no necessity to move today.
- H.M.Jr: No, but the way I thought I was going to do this thing - I mean I thought of doing something which I had never expected to do before, and that is to force the French hand.
- White: The danger of doing that, Mr. Secretary, is that the doubt in your mind and the doubt in all our minds is that that will be sufficient, and if you make any insistence upon something unaccompanied by other factors which will insure its success, then I think there is some reason why it shouldn't

- 6 -

be done. If you had in mind some thought that in addition to that which would insure it....

H.M.Jr: Well, what?

White: Well, what I would have to suggest, I suppose, is not practically feasible, but then I wouldn't suggest it.

H.M.Jr: Well, go ahead, what?

White: What would be in my mind - what would be a bold stroke, and I think a desirable one, would be a fairly extensive long time loan coupled with certain conditions made by the Federal Government. Gold loan by the Stabilization Fund.

H.M.Jr: Such as - what are the conditions?

White: Well, some reorganization possibly of the Bank; some question of technical matters which would insure not only - which would insure a restoration - partial restoration, at least, of confidence; possibly certain questions with regard to their social legislation.

H.M.Jr: Well...

Knoke: Lobbying in other nation's affairs. And, what is more, it is a - is it politically possible to make an advance to the French?

White: Buying francs. A loan, no.

Knoke: I say politically. Take the Hearst campaign on...

Lochhead: Yes, do you remember the thing they are - they keep talking that we are financing the French Government.

H.M.Jr: No, all I was thinking of was this. After all, I think it is perfectly proper....

Lochhead: Mr. Morgenthau, I think... Excuse me.

H.M.Jr: Will you hold your thought a minute?

All I'm thinking is this. You can take a 21 year old

- 7 -

boy and say, "Now look here, you're of age, you've come into your income. You have your own money. I can't as your father any longer hold the purse strings. But I can say to you, my dear boy, even though you are twenty-one and you have your own income and you are free, white and twenty-one, that I would conduct your financial affairs along these lines. Now, all I can do is point it out to you, but I can't make you do it."

Now, all I can say to the French is - if I go that far is - just the way Mr. Hoover refused to see that for two years he should get off gold and devalue, refused to see it; it took a political upheaval in this country to make America see it - "Now, here, all I'm going to suggest to you is that the thing for you to do is to quickly devalue and then make corollary moves which you yourselves know are best." Now, that's all I have in mind, and no one can object to that. Do you think so, Knoke?

Knoke: No, but I just want to....

Lochhead: Here's the way I feel about this. I feel this way...

White: That's wholly gratuitous advice, Mr. Secretary, I think, for this reason: that they know they can do that.

Lochhead: There's something on that....

H.M.Jr: Now wait a minute. Just let's get our New York - you know, you've got to treat the New York bankers with extra consideration. I mean don't let's get...

Knoke: I just want to say this, that you are - your suggestion is going farther than what, according to reports at least, a fellow like Baudouin has set forth as a program.

H.M.Jr: Who's that?

Knoke: Baudouin, the General Manager of the Bank of Indo-China, who has been suggested as successor to Labeyrie.

H.M.Jr: And Labeyrie is the head of the Bank of France?

Knoke: Yes. Baudouin is reported to have stated he would accept an appointment under certain conditions. The first of them was immediate stabilization at present level, no further devaluation. Secondly, full payment for gold, even to those who have turned it in before at the lower price. And thirdly, lowering of the tariff. Now, I should imagine - that looks to me like a program that has hand and foot. Whether it is possible I don't know.

H.M.Jr: But in that he says nothing about further devaluation?

Knoke: He claims - at least, I assume that he feels that prompt stabilization, together with the other two things, would turn the trick for France.

H.M.Jr: Well, he's wrong.

Knoke: Well, maybe he is. I don't know.

H.M.Jr: Well look, I compared the French situation very much to the fall of '33 when Mr. Roosevelt was in here. Now, the more you study the fall of '33, the more you realize that the people that Mr. Roosevelt put in the Treasury couldn't run the finances of this country. They just couldn't do it. I mean - you know the first Liberty refunding that we had was a failure. . You couldn't borrow any money. You couldn't borrow for more than thirteen months. You paid two and a quarter percent for the thirteen months. And Mr. Roosevelt was right up against it. He had this tremendous deflation after that rise and he had to make a clean sweep of his Treasury.

Now Mr. Blum has got his social legislation, which at the distance - most of it I'm in favor of; but he hasn't been able to handle his finances. Now that's his big problem. And - just one second - the people often who are so terribly close to the thing... After all, when Blum came in, he went in

- 9 -

on a program - on a platform of no devaluation, and we here more or less had to show it to him, that it was a question not of internal policy but it was an international matter, and on that basis he switched.

And all I am saying is that I think it is something that often - one doctor can't analyze himself, I mean. If a doctor is sick, he always gets another doctor. No good doctor will prescribe for himself.

Now I'll keep quiet for a few moments.

Lochhead: I was going to say we are speaking here about devaluation; we said that under the tripartite France has a right to go down X rate percent.

H.M.Jr: I wouldn't go that far.

Lochhead: We'll say they can go down eight percent.

H.M.Jr: Don't go beyond the eight percent.

Taylor: They can, under the tripartite agreement.

H.M.Jr: If she gets our permission.

Taylor: If conditions are such....

H.M.Jr: No, you're wrong on that.

Lochhead: We talked the tripartite on specific figures.

H.M.Jr: What was it, from 24 to 34?

Lochhead: That was the basis we agreed on.

H.M.Jr: What?

Lochhead: That was the basis we agreed on as a specific limit. But France did pick the middle rate to support and they have supported that middle rate and everybody has gotten used to that middle rate. Although they have the right to go down the eight percent, I don't think France feels free to go down that eight percent after having set the middle rate and held to it.

- 10 -

Now, I think the ideal approach would be that we and Great Britain would have no objection to them going down to the lower rate if they thought the time was right and they took other action which would fortify their decision to do so. I mean in other words, it is not a question of our telling them to go down, but say, "We feel that - we are not going to object if you wish to go down there."

H.M.Jr:

Archie, you were right two weeks ago, see? Two weeks ago, they got that fresh forty million. You could talk about it that way. When I tell you that at the end of ten days they'll have nothing left, the time - to use the expression - to be "mealy-mouthed" is gone. And I think the time has come to say to these bozos, "If you're going to save yourselves - we can't save you, nobody can save you - if you're going to save yourselves, you've got to devalue the limit of the eight percent and then take certain steps which you know - which you know better than we do, to gain the confidence of the capitalistic system in France. Now, if you're going to stay on a capitalistic basis you've got to satisfy those people. I don't know what those things are. I don't know French politics. But there's certain things you've got to do."

And I'd say to them - I don't mind saying to them, "Sitting here, three thousand miles away, I consider your case hopeless. You're through. You're absolutely through." And I have never said that about the French, and these people have come over here and I've said they're much too pessimistic. But the thing that's got me is these darn French statistics. I mean Belgium, their exports increase; Holland, their exports increase; Switzerland, their exports increase. France, down! China, their exports increase. Everybody's doing more business except France. They've got nothing out of this thing and their price...

Knoke:

Well, there are also certain bright features. You will agree, for instance, that French revenues have picked up; moderately, it is true, but they have picked up.

- 11 -

Now, as regards giving advice to France, my personal feeling would be not to give - last of all to give it to a nation as proud as France. But I think any other - what any other government or outsider can do, or in our case what we can with perfect propriety do, is to tell them that devaluation to a lower level, to the 35 percent level, will be perfectly all right with us.

H.M.Jr: Listen, Mr. Knoke. I'm trying to think of some country, small country - I can't just think of it. The Austrians are very proud - very proud people. So are the Persians. They are so proud that when their Minister is arrested and he beats up a cop, they don't recognize it; they withdraw recognition of America. We don't have a Minister from Iran any longer, they are so proud.

Knoke: Yes, but...

H.M.Jr: Now wait a second. If we hadn't time and again come to their rescue, then the French could say, "What right have you got to talk to us when all the time during the last two years you never would raise a little finger?" But I'm perfectly willing, if the President approves it - "I can talk to you like a Dutch uncle because I was always willing to come and came quickly." Supposing they beat the press and say, "You've insulted us." Now wait a minute. They say, "You've insulted our national pride." Well, as the expression goes, "And so what?" What of it?

Knoke: Well, except that in that case...

Taylor: They won't say that.

H.M.Jr: They won't say that? That's fine.

Taylor: What you'll do there - the minute you put yourself in that position, they'll say, "Well, we'll do that, but we've got to have something on the line to help us do it."

H.M.Jr: No, I disagree with you again.

- 12 -

Taylor: I think that's what they'll have to say.

H.M.Jr: "All right, then the tripartite agreement is busted. We consider you a bankrupt fourth class nation. We won't do business with you. We can't bother with you."

Knoke: Yes, but it won't help us either, Mr. Secretary.

H.M.Jr: Look, you've got - somebody's got to shock those people into realization to face this issue. Now, just as you say, the new Governor, the man who's mentioned for the new Governor of the Bank of France - in his program he doesn't mention further devaluation.

Now, somebody asked me - we had a meeting the other night in preparation for my going up to Harvard. They said, "How did you arrive at \$35?" I said, "We were fortunate to strike \$35 an ounce for gold and by God it's worked." Now, after all, if it hadn't worked we would have had courage to go to - what was it, \$41.34 - is that what it was?

Lochhead: Yes.

H.M.Jr: We would have had courage enough to go to \$41.34. The fact that \$35 pulled us out of the depression is the seventh wonder of the world. And if the boys asked me the test - "How did you hit it?" - I'd say, "It was just Roosevelt and Morgenthau luck that we hit \$35, and for three years by God it's worked."

Now, they hit at six cents, or whatever the thing is, for France and it hasn't worked, and somebody's got to shock them into the realization that they didn't do - they haven't got the right combination.

I keep saying to the people... I know enough about business. It's the rarest thing that a business pays, isn't it? There are very few corporations that make money. And when you do make money and you try to break down why one corporation makes money, it is the very delicate balances between profit and loss. Some have got it and some haven't. And we have this very delicate thing in America that Roosevelt

- 13 -

got the combination to, and America is going ahead better than any other in the world.

Incidentally, you don't see any of the New York Anglified press publish the facts about the cheapness of our financing, but for two years they rubbed my nose - "Why can't you finance as cheaply as England does?" Why do the New York papers - because they are all Anglified and for two years they said, "Why can't Morgenthau finance as cheaply as the English do?" Now we've got the combination and the French haven't.

White: May I raise some objections?

H.M.Jr: You can raise three.

White: One, that's all I want. I am thoroughly in sympathy with you in regard to hurting French feelings. I don't think that is a matter of any importance, by virtue of our relations.

H.M.Jr: May I just interrupt you? I haven't - here three years and I haven't insulted anybody yet. But if I find... But just remember that in three years I haven't insulted any nation yet. Go ahead.

White: But I feel this way. I'm not at all certain, and as I said, I don't think you are, that a further devaluation of eight percent will correct the situation. There must be additional factors. I further feel that they know and they have no doubts that they can go down the eight percent. We can't do anything but agree. They may ask us, but there's no doubt in their mind that we'll agree to their going down, because that was the original understanding. Therefore, by our telling them we are not giving anything additional, though we may be very nice in telling them - but if you say, "We advise you to go down," without having something in mind to come definitely to their assistance, I don't think we are helping the situation.

But I'm more interested in something beyond that. I think we ought to regard that notes the franc situation, but as the dollar situation, and I think

- 14 -

we've got something definitely at stake in connection...

H.M.Jr: What do you suppose I'm worrying about?

White: Well, I don't think worrying is enough. I think we've got to be prepared to take....

H.M.Jr: What do you think I'm doing this for? My whole purpose is that I see right before my face that the tripartite agreement is busted. Now, what can I do?

Taylor: Well, what are you prepared to lay on the line? That's what it comes down to.

White: I feel we ought to be prepared, for several reasons, to lay something down on the line. Then, if you are prepared, you can say, "We'll be prepared to cooperate if you do this and that as you ought to do this and that." Then I think we would be taking a bold position - along with England, if you like; without England, if you don't like. We'd be taking a bold position, and that bold stroke at this moment, coupled with devaluation, I think, can save the day.

H.M.Jr: I have an answer.

White: That's what we've got a fund for.

H.M.Jr: Well, I have an answer.

White: You have an answer?

H.M.Jr: Oh sure.

Taylor: Well, that has got to be part of it. Otherwise, you can't make the first plans.

H.M.Jr: I mean I've got the answer, but...

White: It seems to me this is no time, as has happened again and again and again in international relationships, to try to approach this problem in a small way. There must be risks, there must be boldness, there must be courage. We've got the

- 15 -

funds to do it and we've got the power to do it. The occasion is ripe, and I think if it is approached in that way you can pull the chestnut right out of the fire. There's a risk, of course.

H.M.Jr: There's only one answer. There's only one answer on this whole thing, and that is for the President to call five or six of these countries here to Washington and lay down the law and have a disarmament program. Now, that's what's busting all these fellows and that's the whole answer. Lending these fellows fifty, a hundred, three hundred, a billion dollars, doesn't make a bit of difference as long as this armament race is on. If the President of the United States would take the thing and say, "I'll call these boxos here and just knock their heads together and make them quit this armament"....

Miss McCormick - what she says, the last paragraph, talking about Germany: "The other is to utilize a great part of this raw material for productive industry. If this was done, it is promised by those who know that the country is in a position to increase its exports by a billion marks yearly."

I mean it's the whole thing.

Knoke: You put your finger on it.

H.M.Jr: That's the whole answer. Lending these fellows a couple hundred million dollars against gold, - it would be gone in a short while. The only answer to this thing is if the President of the United States will call five or six of these fellows to Washington and lock them in a room and say, "You fellows have got to quit arming."

Knoke: Pardon me, but I think Mr. White's plan is not to lend against gold but to lend against paper.

White: If you can lend against gold, by all means. That you can do any time. What I had in mind is to lend against paper and take the risk. I said "providing there are conditions." I don't say to lend without conditions.

H.M.Jr: This whole thing goes back to one thing, this racing

- 16 -

to arm, doesn't it? And that's what's busting this world. And I've got to come to this point: the world is just going bankrupt, and this French thing is just - the French, strange as it may seem, may crack before the Germans do, and this whole thing gets back to this race.

Now, I want to lay all my cards on the table, and what I told the President was this: that through the French - getting them to devalue - it gives them another five or six months' breathing spell until we can call this disarmament conference, and that's what we need. We need a breathing spell; otherwise, the French will crack. Two months - a month, two months, they're gone, Blum's gone, God knows what kind of a government you get, and then it's too late.

- White: Well, my point is if you want a breathing spell you might get one by devaluation; you probably will. But I say you insure that breathing spell - there is so much at stake in this whole business that I don't think we ought to cavil at the few hundred million dollars or possible loss of fifty or a hundred million dollars, and I think if you could accompany that devaluation...
- H.M.Jr: You can't make them a loan. Under the law, you can't make them a loan against paper.
- White: Yes, you can. Certainly, definitely. The Stabilization Fund definitely can.
- H.M.Jr: Well, if you can I wouldn't want to.
- Taylor: That's why you have to be careful. You say you won't make the loan; therefore, you've got to be damn careful about what you say.
- H.M.Jr: Well, I wouldn't make it because it is just throwing money into the Atlantic Ocean.
- Taylor: Sure, but that's what it comes down to.
- H.M.Jr: But to keep this French ship going for three months, six months - if they devalue, plus certain moves

- 17 -

which are very obvious - if they take this thing, I mean, and on top of that if the President would call a Washington conference like in 1921, would call the different nations and have a disarmament conference, we'd get some place. And if he doesn't do it, as far as I can see - I mean you've never heard me talk as blue as this, have you?

Taylor: I don't think you can talk too blue.

H.M.Jr: I think we're through - not we, they - Europe.

White: When you speak of disarmament, you also have in mind you are speaking of only one source of the trouble. There is a more fundamental difficulty and that is the political one, which is coupled with armaments. So when you speak of a conference you are assuming, with considerable optimism, that you will be able to check the basic political differences.

H.M.Jr: Listen, you stop - I'm not even talking about freezing the armaments, by any means; I'm talking of real disarmament. You stop these people from this armament race and put their money to peaceful purposes and a lot of these political things which loom so big today would not be nearly as important.

White: I agree.

Taylor: Well, the natural question to that is: we call the disarmament conference; "All right, boys, that's fine" - now what'll you do?

H.M.Jr: I've had this up with the President....

Taylor: Just as we advise the French here, "You've got to be prepared to go through with something." Now, what would it be?

H.M.Jr: Well, I'm telling you just in this room I've had this discussion now with the President for three weeks, and much to my surprise, every time I bring it up he's encouraged me. I mean I've felt that I was out of my line, it was out of my backyard, but he wanted

- 18 -

me to go ahead with this thing and for the three weeks I've been pressing him along this line, that this is the only hope, and he is not afraid of it.

Taylor: No, I think you're absolutely right, but...

H.M.Jr: Of course he has to have a plan, Wayne, but he's been thinking about it and the thing has been crystallizing in his mind, and the more he thinks of it the more he likes it.

Taylor: But it may be either opening our markets or some other method of giving these boys raw materials.

H.M.Jr: He's got a plan; he's got a plan. But see, he hasn't got a plan as to their political troubles. Those things they'll have to settle between themselves. But as to the economic-monetary thing, he's got a plan.

Lochhead: Is his idea sufficiently crystallized that there might be a possibility at the time the French went down to this devaluation - that there might be some preliminary talk about this conference?

H.M.Jr: That's what - I'm beginning to think that the thing should be hooked up with that.

Lochhead: Then if you do that I was wondering - you could do this now and then arrange the other in the summertime.

H.M.Jr: I think when this thing happens, he ought to hook this thing up with an announcement that there is going to be such a thing. Then that will tide the thing over for five or six months - that is, if he said, "All right, do this thing and we'll get together in September."

Knoke: What would be the procedure to make sure first that the fellows will sit in on a disarmament conference?

H.M.Jr: I suppose he'd have to send out to three or four countries and say, "Now, if I ask the following countries, would you, Mr. Baldwin, be willing to come to the United States? Would you, Mr. Mussolini? Would you, Mr. Hitler, come to the United States?"

Knoke: Yes, I think that would be necessary as a first step.

H.M.Jr: See? "Would you come?"

White: Mr. Secretary, isn't it...

H.M.Jr: "Would you, Mr. Blum, come to the United States?"
And then - they keep shifting - Hyashi - who's the
fellow in Japan? Is it Hyashi? They keep shifting.

White: Isn't it evident that if that is enough to maintain
them for five or six months, as you hope - if it is
enough and if you want it to be maintained until
this conference, then I say there is no risk in the
extension of a loan. The only risk in the extension
of a loan occurs if this condition breaks down. There-
fore, if you want the condition not to crack between
now and when that conference can take place, then the
loan can do only good because it will not involve any
risk.

H.M.Jr: Listen, Harry, if they got seven hundred million
dollars plus an announcement of this conference -
seven hundred million francs - the thing will go.
But I can't help it; my whole upbringing, my whole
background, rises up in protest against making a
loan against French paper. I can't do it; I just
can't do it.

White: Seven billion. Seven to eight billion.

H.M.Jr: I can't do it.

Taylor: If you could combine the two things - the French
going to the lower limit and the announcement of the
calling of a conference, that would do the job. Of
course they shouldn't be connected in the minds of
the public.

Lochhead: And they shouldn't be too far apart.

Taylor: They come out practically the same day, but they
shouldn't be connected in the minds of the public.

Lochhead: The public will do their own connecting. I mean
you'd have to have the time figured out.

- 20 -

- Taylor: It could happen the same week. If they could happen the same day, it would be ideal.
- H.M.Jr: Well now, I just want Knoke for a minute. Now, Knoke, you don't sit in here every day. In the first place, am I too much alarmed?
- Knoke: No, you can't be too much alarmed.
- H.M.Jr: I'm not too much alarmed?
- Knoke: All the information we have certainly bears you out.
- H.M.Jr: Now, whether - if Blum falls, whether the Socialistic government sticks or whether it goes Right doesn't make much difference, does it, because if the Right government came in they couldn't get sufficient support to last a week, could they?
- White: You'd have a series of conflicts.
- Knoke: I don't know that I would go that far. I think to the extent that the trouble seems primarily political, much more than economic, it seems to me - furthermore, to the extent that the first thing that is necessary is the reestablishment of confidence, I wonder whether a change in the government in France wouldn't bring about that confidence, just as you say the change of administration here in 1933 brought it about in the United States.
- H.M.Jr: But they've got their "New Deal" administration now. They've got a real New Deal.
- Knoke: Maybe they've got too much of it; I don't know. Maybe what they need is infusion of new blood, but a little more conservative.
- White: No, the situation is much more unstable there, and a shift back will merely accentuate a good deal of the internal political difficulties.
- Knoke: What do you mean by a shift back?
- White: A shift over to the conservative side.
- Lochhead: No matter what government was in there, you'd still have your armament race, so I say a temporary shift

- 21 -

in the government over there just now might mean they could save themselves for a year instead of three months or something like that. But you haven't got down to the bottom of the situation no matter what government is in, under present conditions.

- Knoke: No, I don't quite agree with you, because I think France's struggle today is due, to a great extent, to the methods she has applied since last September. Last September, at the time of the tripartite agreement, I think there was sound reason to assume that it would help France, but she seems to have - Auriol seems to have been successful in making every mistake that he could make as he went along. His whole method has been wrong, with the result today that their confidence, which was already shaken in September, is completely gone. I think a change, not necessarily - I don't mean a change from the radical to the extreme right, but a change, for instance, in the Ministry of Finance, I think, would go a long way toward putting France back on somewhat more solid feet.
- Taylor: You have to have, in order to answer the situation, however, the ceasing of this armament expenditure, because otherwise it is just a question of time.
- Knoke: Certainly.
- H.M.Jr: You (Taylor) agree with me on that?
- Taylor: Yes.
- H.M.Jr: I mean you're putting your finger on it.
- Taylor: You can stall here, create a certain amount of confidence, but you're not going to answer the question.
- H.M.Jr: Now let me just shift a minute. Supposing nothing happens, Knoke. Supposing they don't devalue. Supposing they go goodbye and there is exchange control and chaos, and so forth and so on. How are we going to manage the pound and the dollar with the French out of the picture, the French gone?
- Lochhead: It would...

- 22 -

H.M.Jr: Just a second. Give Knoke a chance.

Knoke: Well, that's a - that wouldn't perturb me particularly, because I think the last six months have proved that there is willingness and desire between ourselves and Great Britain to cooperate. I think if that continues we could still keep on going, even with France out of it.

H.M.Jr: Well, how would it work? I mean just do a little crystal-gazing. How would it work? France is out of the picture. She's busted, finished. How would it work?

Knoke: We'll probably limp along.

H.M.Jr: I mean - I know, but I'm just - would the pound go up, would the pound go down? What would happen?

Knoke: Mr. Secretary, you can't - even with this thing continuing, you can't say that sterling will go up, sterling will go down. I think nobody's wise enough to answer that even under present conditions, leave alone a complete change.

H.M.Jr: I mean do you look with trepidation and fear towards trying to manage the world's currency just between England and ourselves? Do you think we can do it?

Knoke: Well, of course we can do it. France's contribution has been comparatively - as a matter of fact, she has contributed nothing. She might have contributed if the tripartite agreement had brought about what was hoped of it, a restoration of France. But France has contributed very little in the last six months; has been a liability.

H.M.Jr: What do you (Lochhead) think?

Lochhead: I certainly feel that if some emergency does happen with France, we should immediately get in touch with the British and say, "Well, we think it is very necessary to keep this, what is left of the tripartite, going. Are you willing to play along same as we are willing and not to try to force any rates, but to try to keep things steady, to use our stabilization funds to do so?" As I say, I certainly feel we

- 23 -

shouldn't hesitate in getting in touch with the British even if they don't get in touch with us. I think there shouldn't be any delay. We simply say, "Here's the rate. We don't see any reason why the pound-dollar rate should change materially, and if you are willing to play along, we are willing to play. It should be beneficial to both of us."

H.M.Jr: Well, do you suppose - the French distress money has pretty well left France by now, hasn't it? I mean this thing that we are talking about - the French capitalists are certainly a great deal more frightened than I am, and this money which has been coming here in such large quantities - a great deal of it is French money; and I've noticed the last day or two this thing has been sort of quieting down a bit, and certainly there can't be an awful lot more that is going to come out.

Knoke: Well, I don't think it's entirely over, and I would say that is borne out by the way the French have gone; they are selling off. Who is the primary holder of French francs? It's the middleman in France. And the way the rates go, to my mind, indicates that the middleman is still selling.

H.M.Jr: Well, sure.

Knoke: All right, that being so, he is taking flight either into foreign currencies or possibly into commodities. I think some two or three weeks ago we looked into that and found that, from all indications, the French were turning into commodities rather than into foreign exchanges at that time.

H.M.Jr: You (White) haven't got - couldn't lay your hands quickly on the charts which show English bonds, French bonds, and our commodities, could you? I could take it over with me.

White: I was trying to think whether it was up-to-date; I don't know.

H.M.Jr: Well, see if you can. I want English bonds, French bonds, and American commodities.

If they went "caflooey," then they'd put on exchange

- 24 -

control and the Frenchman couldn't get his money out.

Taylor: He'd be able to get some out.

Knoke: That reminds me of - who was it the other day? - oh, Niemeyer said, "Schacht's proved one thing; that is that exchange control cannot work." There's a great deal of truth in that, because if the Germans, with all their discipline and all their regulations, can't make this thing watertight, there isn't a nation in the world that can. And the French certainly can't.

Lochhead: The French would be the last ones to make a success of it.

Knoke: We would be the last ones, I think.

H.M.Jr: Have the Germans - I thought they regulated their foreign exchange pretty well.

Knoke: Well, to all....

Taylor: Better than anybody else, but...

Knoke: Yes, better than anybody else by far, but still the - when this fellow from the Reichsbank a couple of months ago - he made what I thought was a very amusing remark in talking about Germans going into Switzerland. He said, "We've followed this. We know about it every time a fellow goes. We say, 'Well, he's going to visit his capital in Switzerland.'" "

Lochhead: Well, you know what Cochran said, don't you, about the time the German hockey team was playing the English hockey team in London. One of the cruise lines made special rates, but even then they were surprised at the number of Germans that made the trip. They never got out to the game. They dashed to the banks. It was the only chance they'd gotten to get out of Germany in a couple years.

Knoke: You can't follow - have a policeman back of every citizen.

H.M.Jr: They pretty near do.

- 25 -

Knoke: All right, but even then it doesn't work.

H.M.Jr: Well, at least you fellows know how I'm thinking. I don't think anybody's in disagreement. What?

Taylor: No, I don't think so. The thing is if the French situation goes to the worst extreme, it will simply remove her from being a cooperating member in good standing in our group over into another group. But there's no reason why the British and ourselves can't continue to cooperate.

Lochhead: Possibly Holland and Belgium would stick in too.

Taylor: Oh yes.

Lochhead: And Switzerland.

Taylor: Oh, Holland and Belgium and Switzerland would stick. It just moves France over into Germany's class.

Knoke: Which won't help...

Taylor: Won't help the world any. But as far as making our problem more difficult, I don't think it makes...

Lochhead: I think, as I said, there is no reason for us to throw the tripartite away.

Knoke: Well, it's a two-party agreement.

Taylor: That's all it amounts to anyhow.

Knoke: Better, because it keeps the channel open for the exchange of opinions.

H.M.Jr: I'm going over, gentlemen, and if you'll be around - if you (Lochhead) will take over Mr. Knoke, and I'll be back. I've got a call in for Cochran at eleven and I'd like to see you then, and everything will go by the board until then.

MEETING ON FRENCH SITUATION

February 26, 1937
11:00 A.M.

Present: Mrs Klotz
Mr. Taylor ✓
Mr. Lochhead ✓
Mr. White ✓
Mr. Knoke ✓

H.M.Jr: I've gone so far, I've got to go a little bit further. The President is just about as pessimistic as I am, and the only suggestion he had to make is to send word to Mr. Chamberlain very, very quietly and secretly whether there is anything that Chamberlain and I might do together. So I've asked Sir Ronald Lindsay to be here. He'll be here at 11:30. I'll ask that he send word to Neville Chamberlain - is there anything that he and I might do together. Huh?

(On phone) Hello, Cochran. (Record of conversation follows:)

Friday
February 26, 1937
11:03 a.m.

307

HMJr: Hello, Cochran?

Cochran: Yes, Mr. Morgenthau.

HMJr: I have decided that - in view of this debate this afternoon -

C: Yes

HMJr: - that I'll wait now until we see what happens. And I understand Mr. Blum is going to talk Sunday?

C: I'm not sure what time he'll talk. There's several speakers. Sometimes he lets them all finish before he speaks, see?

HMJr: Well, we'll wait. And when you get it all - go into great detail and get it all.

C: Fine

HMJr: And then, Saturday, send us an interpretation of what the French and English papers say, see?

C: Yes

HMJr: Both Saturday and Sunday so I can have everything, as much as possible, by Monday, see?

C: All right.

HMJr: And - but I'll sit tight now, waiting for this debate.

C: - all right.

HMJr: Have you got any more news since this morning?

C: No, I've dictated a lot of the telegram. I'll get it off yet tonight.

HMJr: Well, you'd better tell it to me because I won't -

C: - I have - there's nothing new on the market situation today at all.

HMJr: Nothing new?

-2-

C: No - it's fairly quiet.

HMJr: All right.

C: And the people - with whom I talked particularly, especially the under look for a clarification of this thing in about two weeks.

HMJr: Yes

C: Because that's at about the time this fund would be exhausted at the present rate.

HMJr: I see.

C: And I'm not sure that I made it completely clear this morning, the fact that this is a political situation fundamentally, here now.

HMJr: I don't get that.

C: I mean, when you were put in there -

HMJr: When what?

C: I say, when you took office -

HMJr: Yes

C: I mean, your Chief knew that he was to be in for three more years.

HMJr: Yes

C: And he could tell you to go ahead on the technical way that he thought - that you together thought it ought to be run.

HMJr: Yes

C: Here these people have to watch every step, you see?

HMJr: Yes

C: Lest they be thrown out.

HMJr: Yes

C: And it's just that political desire to retain power -

HMJr: Yes

C: - that's preventing certain things which ought technically to be done.

HMJr: Yes

C: I mean, that's the difference.

HMJr: Yes

C: But I'll try to explain everything in the cable -

HMJr: All right.

C: And follow up tomorrow and Sunday -

HMJr: All right.

C: - with an analysis of the debate.

HMJr: All right.

C: I'll try to make good comment.

HMJr: All right, thank you.

C: You'll be back Monday, will you?

HMJr: Pardon me?

C: You'll be back in Washington on Monday?

HMJr: Oh yes

C: On Monday?

HMJr: Oh yes - and your cables, I'll have them brought up to Boston to me.

C: I see.

HMJr: Whatever you send, I'll have them brought up to Boston so I have them.

C: Well now, I'll get off this one tonight without fail.

HMJr: All right.

C: And I hope you have a good trip.

HMJr: Thank you, - goodbye.

- 2 -

- White: There's no thought in your mind of indicating in any way to Chamberlain what you have in mind, but merely asking him...
- H.M.Jr: I mean is there anything he and I can do together? He doesn't - we know from the French that Chamberlain doesn't tell us everything that he does, because we get it from the French. Huh?
- Knoke: Yes.
- H.M.Jr: He doesn't tell us everything he does.
- White: Mr. Secretary, you made a statement of fact that I want you to be sure on. You said that French foreign trade has not increased. Did I understand...
- H.M.Jr: That exports....
- White: You must be thinking in terms of gold, because in francs it has. I'm making up a table that will be here.
- H.M.Jr: I thought on that weekly chart it showed French exports falling.
- White: That may be true.
- Knoke: Imports have increased more than exports.
- H.M.Jr: The balance of trade has gone against them.
- Taylor: Their exports haven't increased relatively.
- H.M.Jr: No, I'm thinking in terms of balance of trade, and their balance of trade is worse off.
- White: You're correct in that. That's the significant thing with reference to this exchange situation.
- H.M.Jr: I'm thinking the balance of trade is worse.
- Knoke: That's right.
- H.M.Jr: You know, the thing that interests me is the way our commodity price since the month of January has leveled off. Have you noticed that?

Knoke: Yes

H.M.Jr: What?

Knoke: What is it? 206?

H.M.Jr: I can't tell on this chart. It looks like 207. But it's between - it hit 210 about the 15th of January and since then it went down to 205. It's between 205 and 210 for two months. But look at that rise.

Knoke: What month?

H.M.Jr: Look at that rise there from...

Knoke: What month is that?

H.M.Jr: October first.

Lochhead: November first.

H.M.Jr: November first. Look what's happened; and then it's leveled off. From August to October - November first - it was fairly steady. Then it took that sharp rise to the first of January; then it's leveled off again.

Knoke: Yes

Lochhead: What's holding it down?

H.M.Jr: I think that's good, don't you? What?

Knoke: I'm not a chart reader, but that's the way it affects me.

H.M.Jr: Well, I don't want to see our prices go up. I mean certainly, White, while it was going up there we were losing ground in the world market.

White: No question about it. We've lost ground since July. But the loss came - we don't have it in February, January, so the loss came as a consequence of that rise.

H.M.Jr: Now our prices have leveled off.

- 4 -

- White: Then, other prices are rising. Probably the next figures will show an improvement in our position.
- H.M.Jr: An improvement in our position.
- White: Because the other prices in other countries are rising. Our prices right now, I think, will show rather well relative to British and French prices.
- H.M.Jr: But the interesting thing is that our prices and the British prices have been more or less moving the same way.
- White: That is because we are very heavily weighted with international commodities.
- H.M.Jr: For the first time our prices and the British prices seem to be moving together.
- White: Not for the first time.
- H.M.Jr: Well, I wasn't conscious of it.
- Well, I don't see - what's today's situation, the 24-hour situation?
- Lochhead: It's quiet. I've just been discussing with Knoke in there - I mean any possibilities over this week-end and what we should be prepared to do. I think as far as we can see we are all set to take care of anything in the immediate future. I mean there are no further steps that we can take just now under the present situation.
- Knoke: Well, the Secretary is doing just what we were hoping he might do but were not too sure that he would.
- H.M.Jr: What's that?
- Knoke: Rather than wait until the French bubble burst, to talk to the British before. I mean not be - it doesn't have to be today or tomorrow - just rather than wait until the last moment; because I'm always afraid we might miss a train at the last moment; you have a wide fluctuation and nobody knows what

- 5 -

to do in the face of sudden developments.

H.M.Jr: Well, I can't do anything more than - I mean I'm burning myself out physically. I can't do anything more than that. I mean by not leaving a stone unturned.

Knoke: By seeing the British Ambassador I think you are just doing what we were hoping.

H.M.Jr: All right. Well, I don't see anything else, Knoke, right now. Thanks for coming down.

Knoke: So I'm through.

H.M.Jr: You're through. You can catch the 12 o'clock if you want to.

Knoke: I think I'll fly down if it's a nice day.

Friday
February 26, 1937
11:03 a.m.

314

HMJr: Hello, Cochran?
H. M.
Cochran: Yes, Mr. Morgenthau

HMJr: I have decided that,- in view of this debate this
afternoon -

C: Yes

HMJr: - that I'll wait now until we see what happens.
And I understand Mr. Blum is going to talk Sunday?

C: I'm not sure what time he'll talk. There's several
speakers. Sometimes he lets them all finish before
he speaks, see?

HMJr: Well, we'll wait. And when you get it all through
go into great detail and get it all.

C: Fine

HMJr: And then, Saturday, send us an interpretation of
what the French and English papers say, see?

C: Yes

HMJr: Both Saturday and Sunday so I can have everything,
as much as possible, by Monday, see?

C: All right.

HMJr: And - but, I'll sit tight now, waiting for this
debate.

C: - all right.

HMJr; Have you got any more news since this morning?

C: No, I've dictated a lot of the telegram. I'll get
it off yet tonight.

HMJr: Well, you'd better tell it to me because I won't -

C: - I have - there's nothing new on the market
situation today at all.

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-2-

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HMJr: All right.

C: And the people - with whom I talked particularly, especially the under look for a clarification of this thing in about two weeks.

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C: I mean, when you were put in there -

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C: And he could tell you to go ahead on the technical way that he thought - that you together thought it ought to be run.

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C: - that's preventing certain things which ought technically to be done.

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C: But I'll try to explain everything in the cable -

HMJr: All right.

C: And followup tomorrow and Sunday -

HMJr: All right.

C: - with an analysis of the debate.

HMJr: All right.

C:

HMJr: All right, thank you.

C: You'll be back Monday, will you?

HMJr: Pardon me?

C: You'll be back in Washington on Monday?

HMJr: Oh yes

C: On Monday?

HMJr: Oh yes - and your cables, I'll have them brought up to Boston to me.

C: I see.

HMJr: Whatever you send, I'll have them brought up to Boston so I have them.

C: Well now, I'll get off this one tonight without fail.

HMJr: All right.

C: And I hope you have a good trip.

HMJR: Thank you, - goodbye.

February 26, 1937

The British Ambassador came in at 11:30. Feis and Taylor were also present.

HM, Jr: For the first time I feel that the French situation, financially, looks almost hopeless. Of the 40,000,000 pounds which you have advanced them and of which they have already received 30,000,000 pounds, all of it is gone except 1,500,000 pounds so that in another ten days or two weeks the rest of it will be gone. We have to face the situation. If the French are unable to do something they will drop out of the tripartite agreement. Then what will your Government and ours do under those circumstances?

What I would like -- and the reason I asked you to come -- this is a message from me to Chamberlain and it is with the knowledge and approval of the President of the United States: Has Mr. Chamberlain any suggestion of something that he and I might do together at this time, working together, to help this situation. Up to now I have always been sort of keeping my wind up, but frankly I am very, very pessimistic about this situation.

The Ambassador: The last message we had from Chamberlain, which I think was communicated to you, he anticipated clearly that they would go down to a system of exchange control.

HM, Jr: You might tell this to Chamberlain: that my interpretation of the tripartite agreement is that the French could devalue another 8 per cent.

The Ambassador: Yes.

HM, Jr: We would be perfectly willing to have them do that. That would give them another 7,000,000,000 francs gold. That, in itself, would not tide over the situation unless they make other internal changes, but as far as the United States Government is concerned we would be willing to see them go the other 8 per cent. I have not as yet told this to the French.

The Ambassador: This is telling Mr. Chamberlain your own view on that particular point, but also you do not think it would be very effective unless it was supplemented by considerable measures on their own part?

HM, Jr: Is there something that Mr. Chamberlain and I together might do.

The Ambassador: Yes. Yes.

HM, Jr: That is my sad story.

The Ambassador: That is a very sad story, indeed.
at

HM, Jr: You see/ the rate that they are going, when they get this last 10,000,000 pounds it will last them two weeks at the best. These figures that I have gotten were given to me in the utmost secrecy. Your Government may know them. I do not know.

The Ambassador: This is their Stabilization Fund?

HM, Jr: This 40,000,000 pounds advance which you made them went right into their Fund. Just to make the picture completely black, Holland definitely turned them down on a loan.

The Ambassador: Have you anything in mind to suggest?

HM, Jr: No. It is just that we do not get as good information as you do on account of your being so close.

The Ambassador: From the general tone of Mr. Chamberlain's last message to you I should inferred that at that time he had nothing definite to say.

Dr. Feis: The budgetary requirements or the amount of financing they would have to do between now and the end of the year would be 30,000,000,000 francs.

The Ambassador: Make your calculations as you like, I saw some calculations the other day which came to 450,000,000 pounds, that is \$2,000,000,000.

HM, Jr: This is the way I sum up. Possibly Mr. Chamberlain may know of something. Lacking that, I think the wise thing is for your Government and ourselves to get ready and not wait until we wake up one morning and find

-3-

that the French have put on exchange control, scratch our heads and say, Now what shall we do! Possibly, we can get ready now. It is up to your Government and ours to keep the currencies from going completely smash. I do not feel comfortable sitting here knowing that this thing is coming and making no preparations. As we used to say, "C'est la guerre".

Thank you very much for coming in.

The Ambassador left and the Secretary said, "Herbert, can I add anything more?"

Mr. Feis: No, I do not think so. Do you want me to cable this information over to England? This fellow is such an unsatisfactory instrument.

HM, Jr: To whom?

Mr. Feis: To Atherton.

HM, Jr: No. I think Sir Ronald is not so dumb. My hunch is not to send it to Atherton. He once before bungled up a very important message. However, if you say I ought to do it, I will agree.

Mr. Feis: I have no clear purpose in mind other than that in the event that Mr. Chamberlain would want to discuss it with Atherton, he would have the information.

HM, Jr: My hunch is not to send it to him.

What happened here today I only want you to tell Mr. Hull and nobody else.

oOo-oOo

Paraphrase of strictly confidential telegram 283,
from Cochran, the American Embassy, Paris, February 26,
7 p.m.

The Secretary of the Treasury requested me by tele-
phone Thursday afternoon to telegraph today a summary of
the French situation having particular reference to any
possibility for the present Government to overcome present
financial difficulties.

I called on Labeyrie, Fournier, and Cariguel at the
Bank of France this afternoon. It will be remembered that
the last installment of the sterling credit of approxi-
mately 8,000,000 pounds which was obtained at the end of
January from London bankers is to be paid over today. I
was told in the strictest secrecy that only one and one half
million pounds remained in the French stabilization fund
yesterday out of the 32,000,000 pounds which have been paid
in the four preceding installments. The procedure with
respect to the sterling obtained from London has been
for the Treasury to turn the sterling over to the stabiliza-
tion fund, which credited the treasury's account with the
equivalent amount of French francs. The stabilization fund
has paid the sterling out to sellers of French francs and
thus has kept the rate approximately at 105.15. French
concerns and individuals have drawn on their bank accounts
to obtain the francs with which to buy sterling. In order

- 2 - Paraphrase of telegram 283, February 26, 7 p.m.

to reconstitute their seriously declining deposits, the banks have been cashing their holdings of treasury bills and national defense bonds as they matured. Then the Treasury has been obliged to spend an important part of the francs obtained through the sterling credit in reimbursing the bills and bonds thus presented.

A general idea of the disposition made of the British credit will be had from the foregoing. The credit did not check the run on the franc and it has therefore been necessary to pay sterling out in the market almost as rapidly as it has been received. Three days this week have been fairly easy although there was a heavy demand for sterling Monday, and the market was opening as an active purchaser of sterling this morning when I was at the bank. So the sterling obtained from London has not brought about a recovery in the franc but has merely made it possible for the stabilization fund to hold the rate approximately where it was before the sterling was acquired. Furthermore, the credit has been of no real value to the Treasury since its proceeds have been used toward reimbursing the maturing securities as indicated above. The market knows that the payment today is the last installment of the British credit and it is entirely conceivable therefore that there may be a serious renewal

of

- 3 - Paraphrase of Telegram #283, February 26, 7 p.m.

of pressure on the franc now or within the next few days. It is said that the reason for the let-up during three days of this week has been the fact that francs have been needed for the end of the month commercial requirements.

I was also told that as of yesterday, February 25, there were in the French stabilization fund only 783,000,000 francs of gold. It will be remembered that in a public communique February 4 the Bank of France explained that it had yielded three billion francs of gold to the stabilization fund. The Spanish, I know, have lately been more active than usual in sending gold to the Bank of France. Nevertheless, the only gold holdings of the French stabilization fund are the 783,000,000 francs total mentioned above. The foreign exchange holdings of the fund consist of the above-mentioned one and a half million pounds, to which should be added the 8,000,000 pounds to be received from London today. It can therefore be calculated that, at the present rate of decline, the gold and foreign exchange reserves of the stabilization fund will be exhausted within approximately two weeks.

Replying today to the inquiries of Governor Labeyrie and Under Governor Pournier, I told them that
there

- 4 - Paraphrase of Telegram #283, February 26, 7 p.m.

there was no possibility of Franco obtaining a loan in the United States. Fournier asked if it would not be possible to negotiate a short term credit. I replied in the negative, and gave the same type of explanation I gave the Minister of Finance February 15 as reported in my telegram No. 211, of that date. I told them the only possibility on our market was to obtain a short term commercial banking credit.

I have told you recently of the failure of the French to obtain a credit of a billion francs in Switzerland and a credit of 5 billion francs in the Netherlands. It is well known that both the British Treasury and the Bank of England were opposed to the credit which the French Government obtained in London in January in the name of the French railways and that the city bankers were reluctant to give this credit and did so only because they felt that after granting a similar credit to the preceding French Government, which the present French Government has repaid, they could not refuse the latter. Even so, the London market gave only forty million pounds instead of the 50,000,000 sought by Franco.

Personally I am convinced that in present French circumstances no further funds could possibly be obtained from the British Government or from the London market by the French Government or in the name of one of its independent bodies. As the fact that the French have tried to borrow

- 5 - Paraphrase of Telegram #283, February 26, 7 p.m.

on the Swiss and Netherland markets is becoming known in financial circles, the failure of the Government to obtain even the small amounts sought has naturally hurt its credit further. Therefore, I see no opportunity for the French Government to obtain foreign financial aid.

To date the Treasury has drawn on the Bank of France for 7,500,000,000 francs under item three of the monetary law of June 18, 1936. This total is 1.5 billion higher than I had calculated could be drawn under the authorization to borrow ten billion francs from the Bank of France, when one considers the amount of treasury bonds which are outstanding under this same authorization. It seems to be definite that the Government can obtain no further advances in this category from the bank and that new legislation would be required to authorize any further borrowing from the bank. There is ample authority for the Treasury to borrow at medium terms and long terms and to convert short term obligations into medium or long term obligations. However, such transactions are not now feasible on the Paris market. (While outstanding French Government securities remain at their present levels, any idea of forcibly converting them appears unsound.)

The other possible recourse is to issue short term paper, for which I understand there is still some authorization.

- 6 - Paraphrase of Telegram #293, February 26, 7 p.m.

tion. However, I have reported recently, and again hereinabove, the reluctance of Paris banks to take any more of this paper and the tendency to cash it as it matures in view of their need for funds as their deposits decline. Of course the stabilization fund has power to buy gold from the Bank of France with francs which the fund has. If recourse is had to this process after the above enumerated resources of gold and sterling have been exhausted, the transaction would show up in the Bank of France statement and this evidence of exhausted resources would cause even heavier pressure on the franc. It is likely that as the Bank of France gold went lower, there would be a protest from the conservative and military circles against the depletion of the gold "war chest". However, so long as no legislation might be enacted to stop the fund from acquiring gold from the bank, the fund could continue to hold the franc at its present level until, of course, the gold stock of the Bank of France might itself be exhausted.

At the present time, however, the treasury situation seems to point to an early crisis which cannot await better returns from the now obvious improvement in the economic life and from the expected influx of tourists. It has been suggested that use could be made of various expedients such as having Algeria and independent bodies in France borrow in their own name and make the proceeds available to the French treasury. This is exactly what has recently been tried on

- 7 - Paraphrase of Telegram #283, February 26, 7 p.m.

on foreign markets and has failed. The Ministry of Finance has constantly made the point that these units would have to do their own financing, but it must be remembered that practically all these units carry the guarantee of the Government, all obtain their funds from the same common market, and most of them are already in debt to the Government.

While Blum and Auriol have been trying through their speeches to restore confidence, Jouhaux and other Labor and Extreme Left leaders have been talking about nationalization of banks, of insurance companies, of sectors, and some have even been talking of a capital levy. It is becoming generally feared that in case the Government cannot obtain funds through normal methods it may shortly resort to confiscation of funds, requisition of foreign exchange holdings and perhaps nationalization of banks and other establishments.

There was a tendency some days ago to believe that the Government would show a reversal of its policy and display a more generous consideration of holders of gold and exporters of capital. It was also rumored for some days that Blum might drop Minister of Finance Auriol and Laboyrie, Governor of the Bank of France, and give these key positions to men commanding more influence from the capitalists and the saving people of France. Blum's statements since that time, particularly

- 3 - Paraphrase of Telegram #283, February 26, 7 p.m.

particularly those of last Sunday, have for the present excluded any likelihood that Auriol will be dropped and have further indicated that the "pause" promised by Blum in spending measures will be only a temporary let-up and that the Popular Front program will then be resumed on a perhaps more active scale than heretofore. Instead of freeing the gold market, increased penalties have been established against exporters of gold, since a decree dated February 17 has made the contraband laws apply to them.

It was believed a fortnight ago in certain circles that there might be some degree of restoration of confidence if the above indicated changes were made in the Treasury and the Bank of France and if steps were taken to remove penalties inflicted upon holders of gold, to accept gold at the present market value without penalties as to taxes, octrois, and to remove from the banks, Inspectors of Finance who in recent weeks have been going into accounts for the past five years of exporters of gold and funds, but there is now great doubt whether even these changes and measures would be effective.

Blum seems sworn to carry out his social program. Its cost to industry and the resultant rise in French prices make for general fear that a program too heavy for French finance to bear is involved. Blum insists that he cannot reduce his military expenditures and his program would be completely
reversed

- 9 - Paraphrase of Telegram #285, February 26, 7 p.m.

reversed of public works were to be stopped.

Above all, it must be borne in mind that the entire situation is being dealt with by the French as a political matter and they are not guided by technical financial reasoning. President Roosevelt in 1933 was able to carry through measures to which the bankers were antagonistic and was able to make a complete rearrangement in Treasury which brought effective results. The situation in France is entirely different. The head of the government is not in power for a four-year term, but is judged by his every act and his government may fall unless every step meets with the approval of Parliament.

The Popular Front Government, in power for the first time, is exceedingly anxious to stay in authority. It is proud of the progress which it has made in legislation during its tenure of office and Blum's attitude at present seems not to be one of conciliation. Should he replace Auriol by a Minister likely to command greater confidence, this successor would have to come from further to the Right, which would mean changing the complexion of the government to just that degree.

Flandin is interpollating Blum this afternoon on the Government's economic policies. Blum's reply may clarify the situation and indicate in which direction the trend of the government may be, i.e., whether towards pursuing its

declared

declared policies or towards effecting a compromise with French investors. A report on this debate will be tolographed as soon as possible.

There was indication yesterday that the Radical Socialists who constitute the conservative part of the Popular Front are becoming restive over the Government's social legislation and may withdraw their support if Blum insists on more hastily conceived social measures. It is the hope of my more conservative French contacts that the Radical Socialists will eventually force the Government into policies more likely to restore public confidence.

Fournier told me at the Bank of France this morning that he thought the next two weeks would continue to be a period of hesitation but that the horizon might be cleared hereafter. He said that the Government is still opposed to exchange control. Labeyrie, as I have intimated before, is understood to be in favor of exchange control. In talking with me, Fournier admitted that exchange control would be practically impossible or at least would be quite ineffective in France. He recalled how poor results had been obtained by the attempt to control French capital exports after the war.

It must explain that a bitter feud exists at present between Labeyrie and Rueff. Since they are two officials importantly responsible for the financial and monetary policies of France, including the control of the stabilization fund, this is extremely unfortunate. Rueff favors liberal economic policies and one of the first steps after he assumed office was to have the Bank of France lift all restrictions upon the export of capital. The control had been mild but it had been effective principally in enabling banks to give some excuse for refusing the applications of customers for foreign exchange. Labeyrie has resented Rueff's decision on this matter and feels that he does not have the confidence of business men and is not indifferent to influence with the Minister

- 12 -

Paraphrase of Telegram #283, February 26, 7 p.m.

Minister of Finance.

We might prefer more sympathetic individuals in one or two key positions but it must be remembered that the distribution of important offices is largely on a political basis. For example, Baumgartner, whom we found a most honest and direct negotiator when he was Chief of the Movement of Funds at the time we made the tripartite arrangement in the Fall, was removed from that position and promoted to an inactive post simply because politicians of the Popular Front objected to him on the ground that he represented capitalist interests since his wife belongs to a prominent industrialist and banking family. It seems unlikely that he would be restored to his old post or made the head of the Bank of France during the present set-up.

Most well-wishers of France would like to see Professor Rist given a more active part in the control of French finances at the present time. I have not sounded him out lately but on a somewhat similar occasion when French finances were bad and the government was in danger, he told me very explicitly that he was only an advisor and that he was not fit for an executive position in the government and would not at any time accept one. He was, it is true, at one time Under Governor of the Bank of France but his services then were principally those of a consultant on the technical question

question of revaluation of the franc.

The public official most generally condemned, aside from Laboyrie, is Auriol who in the past has proved such a sympathetic friend of ours. I will admit that my recent interviews with him particularly the one just before I left for the United States and the one upon my return reported in detail on February 13, have done much to convince me that Auriol is not the man to right French finances. He believes that the right and the capitalist class are persecuting his Government. He is ill-advised in his public statements and unfortunately his personal devotion to Blum is so unreserved that he would not venture to suggest or carry out a financial policy which Blum might think hurtful to his own political life. He is not a realist when it comes to understanding foreign sentiment towards France's financial problems but is disposed to believe that in some mystic manner these problems may be overcome by cooperation of the three great democracies.

Auriol in his conversations with me on two occasions has talked of definite stabilization of the franc at its present level, i.e., midway between the extremes provided for by the monetary law of October 1. He has also made statements in public that have led to anticipation that

stabilization

- 14 - Paraphrase of Telegram #283, February 26, 7 p.m.

stabilization may be made at this level. He has practically implied in his statements that the franc would not be reduced to the lower limit permitted by the monetary law. Should the franc now be moved to that level, this would no doubt be interpreted as a further instance of his disregarding former promises.

So long as there remains a margin of possible further depreciation of the franc, there is likely to be just that much stronger tendency for Frenchmen to leave their funds abroad and for speculators to attack the franc. Were the franc to be definitely stabilized at present, I should strongly recommend putting it at the lowest level possible under the monetary law since the benefit of such devaluation is certainly needed by France considering its debt and price structure. This would eliminate the doubt as to eventually moving down to this minimum value. A devaluation at the lowest rate has practically already been discounted by the market. Definite fixing of the franc at that rate now would therefore lack some of the good effects which ordinarily accompany definite stabilization.

It is not my belief that this is a propitious moment for stabilizing the French franc definitely at any level.

In

- 15 - Paraphrase of Telegram #283, February 26, 7 p.m.

In most instances successful stabilization has taken place when actual conditions indicated that a level had been reached and was being maintained easily. This is certainly not the case with regard to the French franc at the present time. A fair repatriation of French capital might result from stabilization, particularly at the lowest legal level. However, I do not believe there would be any rush of such capital back to France, even though some holders need use of their capital and normally most Frenchmen would rather have their resources closer home than have them unproductively on foreign markets.

According to Article Two of the monetary law, the new gold content of the franc should be fixed later by decree of the Cabinet Council; the weight of the franc might not be more than 49 milligrams or less than 43 milligrams of fine gold. There was a profit of slightly in excess of 17 billion francs from devaluation at the maximum values of 49 milligrams for each franc. Reduction to the minimum of 43 milligrams would provide about eight and one half billions and would also release ten billion francs from the stabilization fund if the latter were abolished, or a total of eighteen and one half billion but this amount would be liberated only if stabilization is declared at the minimum figure. The convention between
the

- 16 - Paraphrase of Telegram #283, February 26, 7 p.m.

the Treasury and the Bank of France provided that such proceeds, namely the eighteen and one half billion francs, could be applied only to amortization of the public debt. Therefore, if France should now decree stabilization and take all possible proceeds into the Treasury, these under existing legislation could only be applied to the amortization of the public debt.

It seems to me that certain technical measures will have to be taken before confidence in the French franc and French financial administration can be restored. These should include revision of the gold regulations and removal of penalties on gold hoarders and capital exporters. It will be necessary to stop the inspection of accounts in banks by special agents now engaged therein and of whose activities clients have been confidentially informed by their banks, before such clients will again have sufficient confidence to bring funds back to the banks. Such is the present state of mind that even were these technical steps taken, the investing public would still be reluctant to act, fearing that the government, in view of the strong communistic influence within it, might simply be leading them on and would still take punitive measures against them.

While there certainly is need for a price control in France, such a control is almost impossible in a country which has an exceptionally large number of merchants who
are

are of more than average greed and who are accustomed to adroit evasion of tax and other governmental laws and regulations at every turn.

Devaluation has not been followed by the expected lowering of trade barriers. Strong political opposition is now directed against efforts to get in raw materials at lower rates of duty, the argument being that farmers should profit from the price rise as well as do the merchants and manufacturers.

The reorganization of French railways, which is much needed and which has already been planned, cannot possibly take place and show savings to the government for many months.

The tripartite arrangement made provision for consultation between the three governments and their authorized agencies. The exchange of correspondence reported in my telegram No. 249, dated February 20, 7 p.m., showed that the British and the French treasuries have been in consultation by correspondence. Orally when I was in Washington and by telegram since my return, I have transmitted to the Treasury the inquiries and suggestions of the French Ministry of Finance on which the latter desired American opinion and possible cooperation. The French have never told me that they considered this as constituting the

"consultation"

"consultation" envisaged in the tripartite arrangement. I feel deeply that any consultation we have with the French should definitely be upon technical matters and should not touch upon governmental personalities or political issues. I think also that in case the question of giving advice to the French arises, the British and American monetary authorities should consult each other before advising France. I believe this in spite of the fact that there has already been an exchange of correspondence between the British and French in the premises. In this correspondence the British limited their advice mostly to pointing out that the problem confronting France appears fundamentally domestic. As I recall it from the correspondence the only offer by the British was to remind the French of the facilities for consultation under the tripartite arrangement and to say that they would be willing, if the United States did likewise, to state publicly that there was no objection on their part to devaluation of the franc to the lower limit provided for by the French monetary law of October 1. I have not yet been told by the Ministry of Finance what consideration they have been given to the British views received a week ago.

I may repeat that fundamentally the situation is political and that it is being dealt with principally as a political and not a financial problem. It appears that

the

- 19 - Paraphrase of Telegram #283, February 26, 7 p.m.

the Radical Socialists are letting the Government determine its own fate. In case the Government has a financial crisis within the next few weeks, it is conceivable that the Radical Socialists might work towards a Government nearer the center, which would be disposed to make the adjustments in technical policies and in public officials which are considered best fitted to inspire a return of confidence. The working out of the situation might possibly involve as a first step the definite fixing of the value of the franc by the present government. The second step, if this is not effective, would presumably be exchange control. Possibly the government in its present form might stand until exchange control may be proved a failure. However, there is the possibility that the government, in order to avoid exchange control, may take drastic measures such as the capital levy or nationalization of banks or other institutions.

France, I think, should be left to take these decisions independently except for such technical advice as might be sought by its monetary authorities under the tripartite arrangement. I think it imprudent, however sympathetic we may be with the aims of the French Government, to assume any responsibility beyond the tripartite agreement for advice to the French. Possibly anything further than
this

- 20 - Paraphrase of Telegram #283, February 26, 7 p.m.

this might be publicly announced by the French Government on its taking any steps in accordance with our suggestion or, more probably, at the showdown in case such step proved a failure. The tripartite agreement gave the cloak France desired for a necessary devaluation. The two other powers did not assume to guarantee the franc's future regardless of the policies followed in France. We can correctly continue to cooperate with any French Government but it is another matter to sustain a government when the capital holders of that country have insufficient faith in its economic measures and financial administration.

WILSON

RECEIVED
FEB 26 1919
TREASURY DEPARTMENT
DIVISION OF INTERNATIONAL FINANCE
WASHINGTON, D. C.

BUREAU OF INTERNAL REVENUE
OFFICE OF
CHIEF, INTELLIGENCE UNIT

340

February 26, 1937.

MEMORANDUM FOR THE SECRETARY:

Messrs. McQuillan and Mack of this Service advise me that an active investigation is being made of the income tax affairs of Frank Hague, under the direction of Revenue Agent in Charge Baradel. Mr. Russell, in a conversation I had with him yesterday, confirmed this and stated further that he is now preparing a recommendation to you for the appointment of an agent to succeed Mr. Baradel as Revenue Agent in Charge at Newark, New Jersey. He is reviewing the records of the outstanding men of the Newark Division, and expects to have this complete within a day or two and will bring his recommendation to your office, with the suggestion that it be referred to this office for field investigation.



February 26th

H.M.Jr. went over to see the President at 10:20. When he returned he asked me to call the State Department, Mr. Hull's Secretary, and tell him to call up the British Ambassador and ask whether he personally and the new Financial Attache could come right over.

* * * * *

I saw the President and told him that the French have practically exhausted all of the 30 million pounds that they got on their railroad loan recently and the additional ten million coming to them would only last another ten days or two weeks; that the situation was desperate; that if they devalued another 8% it would give them another 7 billion francs gold profit but that this would not help them any unless the President would call a Disarmament Conference.

The President said that he thought it was useless to call it as the countries would not play ball; that they were up against a stone wall; that the British and French have tried this twice during January and had gotten nowhere even though they had intimated that such a conference would be acceptable to Washington and could be held here.

He then said something which did not make sense to me as he was in a great hurry, namely, that the Germans were counting on stabilization rather than disarmament. The next time I see him I will ask him what he meant.

I told him that since I had spoken to him last night at 7:30 I had changed because I had learned from Cochran this morning that Blum and Flandin were going to have a debate about the French financial situation this afternoon in the Chamber and that we might as well wait until we got the reaction to this debate. He said, "Why don't the French seize all the gold the way we did - that that might help". I did not know the answer but will get it. He said, "The only suggestion I have to make is that you get immediate word to Chamberlain asking whether there is anything that you and he could do working together". He said, "After all, we know that Chamberlain has been doing things with the French without keeping us informed". He said, "You need not let Chamberlain know this at this time but possibly he might have some suggestion to make". I reminded the President that I had sent Bewley secretly on just such a mission and he said, "I know but let's put a burr under his tail". He said if he, the President, made any move on calling a world peace conference it would leak immediately. The President seemed to feel that it was hopeless to call a world Disarmament Conference at this time but that there might be some possibility of Chamberlain and myself working something out together.

I said, "While I am terribly blue about the European situation I wish to report, Mr. President, that our own financial house is in excellent order." He said, "What would happen if the French collapsed" and I said, "Well they would fall into the same kind of position that Poland is in to-day financially and we would just have to forget about them, and the British and ourselves would have to carry the ball alone".

* * * * *

Jimmy Roosevelt told me, and for some reason since yesterday he has taken to calling me the boss, that he has postponed, at my request, the conference with Senator Wagner from 11 Monday to 11 Tuesday and Jimmy and I are to see the President at 9:15 Tuesday morning.

Certainly on the European situation I am doing everything mentally and physically that my person will permit. In other words, I am burning myself out trying to help and if the French collapse and, as I pointed out to the President, the reason I think the Germans have been so quiet recently is that they are counting on the French collapsing - to which he agreed, I certainly will not have anything to blame myself for for not having done everything humanly possible within my power to help France and to try to stave off a European war. The President's attitude is one of complete hopelessness about the European situation.

✓
2-26-37

Herman Oliphant
Secretary Morgenthau

I have studied your report in connection with the offer in compromise to be made in the Isidore Goldberg case. In view of your favorable recommendation, and that of Mr. Manning who handled the case, I approve of the acceptance of the terms of the offer.

TAM.Jr/lhs
2.27.37
26



GENERAL COUNSEL
TREASURY DEPARTMENT
WASHINGTON

Dean

344

FEB 28 1937

My dear Mr. Secretary:

I am now in a position to discuss with you the proposed settlement of the Goldberg case. The amount of loss of revenue suffered by the Government has become immaterial as the proposed settlement is based solely upon the ability of the Government to collect. The loss of revenue which has been computed by Manning is over \$1,100,000. This was determined by a comparison of the commercial invoices with the pro forma invoices upon which entries were made. Goldberg is not financially able to pay any amount approximating this estimated loss, and for this reason it has been felt that it would be a useless task to compute the full amount of loss.

There are two claims against Goldberg and his corporations — that of Customs and that of Internal Revenue. In view of the fact that there is a certain sum of money to be available for the compromise of both claims I think the better manner of handling the matter is to submit the principle of the settlement to you, and if you approve to work out with the Bureau of Internal Revenue the proportion to be allocated to it. The terms of the offer which has been made are as follows:

- (1) The total amount of the offer is \$132,786.79.
- (2) The sum of \$25,000 thereof is to be paid in cash, and to be applied in payment of the fine assessed against Goldberg in the District Court for the Southern District of New York.
- (3) The sum of \$7,786.79 is to be paid by Goldberg, releasing to the Government Customs refunds due him in that amount, and which have been withheld by Manning pending the outcome of the investigation.
- (4) The balance of \$100,000 is to be paid as follows:

The book value of the inventory of I. Goldberg & Sons, Inc., is \$177,960.87. Goldberg has placed a market value upon this inventory of approximately 25 cents on the dollar, or \$44,000. He has offered, subject to our election, to pay on deferred payments this \$44,000 as part of his total offer, or to turn the whole inventory over to us, in which case he would be credited upon the total amount of his offer with the sum of \$44,000, the value which he has placed upon the inventory.

2.

(5) The balance of \$56,000 to be paid in annual installments of \$8,000 each for seven years.

Manning has had this inventory appraised by three examiners of the Appraisers Stores in New York, and they place a liquidation value upon the same of \$99,000. Based upon this appraisal, it is quite apparent that we should elect to take the merchandise as it in reality increases the offer to \$187,786.79. The following security has been offered by Goldberg:

(1) The assignment of insurance policies on his life totalling approximately \$520,000 to stand as security in case of his death before the completion of the payments to be made by him.

(2) The deferred payments will be evidenced by notes signed by Isidore Goldberg personally and by I. Goldberg & Sons, Inc., I. Goldberg, Inc., and I. G. Millinery Corporation. The payment of these notes will be guaranteed by Eurasia Import Company, Inc. This corporation is a going solvent concern, the stock of which is owned by members of Goldberg's family. It was formed in 1935 after the investigation started, and while the capital stock investment was made by members of Goldberg's family, and while we have no legal proof that the stock ownership is otherwise, we believe that the company is owned by Goldberg himself.

The following is the condition in connection with the ability of the Government to collect its claim:

It must be remembered that Goldberg is now serving a prison sentence for these frauds, and, except for the effect a voluntary settlement might have upon his application for pardon, or his proposed application for parole, there is no inducement for Goldberg to offer in compromise any more than the Government can collect by suit, judgment, and execution. The audit made by Gilman & Hirsch, who are reputable accountants, shows a net worth of I. Goldberg & Sons, Inc., of \$203,399.18. Part of the assets shown in the audit is a liability of Isidore Goldberg personally to the corporation of \$24,423.81. This is worthless and reduces the actual net worth of the corporation to \$178,975.35. This includes the inventory at book value of \$177,960.87, hereinbefore referred to. For our purpose, therefore, we can say that the sole asset of the corporation is its inventory. Isidore Goldberg personally has no assets, but is in fact indebted to the Standard Bank of South Africa, Ltd., for approximately \$25,000, upon which judgment has been entered.

3.

The proposed settlement contemplates the turning over of this whole inventory to us. This amount is the maximum which could be prima facie recovered by the Government in an action in the District Court.

In addition to the inventory and refunds Goldberg has agreed to pay the sum of \$81,000.

This additional sum is to be paid through the earnings of Eurasia Import Co., Inc. Prima facie it is an additional payment over and above any amount which the Government can collect from Isidore Goldberg personally or from I. Goldberg & Sons, Inc.

Eurasia Import Co., Inc., as audited by the same accountants, shows a net worth of \$100,259.07. It will be seen, therefore, that the proposed settlement contemplates the taking of over 80 per cent of the net worth of this corporation. It is apparent from the statement of the corporation that it is able to make money, and it is based upon this ability that the additional sum is being offered in compromise, and for this reason the payment thereof is spread over a period of years.

You will note that I have used the words "prima facie" in connection with the statement that the inventory of I. Goldberg & Sons, Inc., is its sole asset. In the formation of Eurasia Import Co., Inc., through a manipulation of inventory and stock holdings, approximately \$50,000 of assets of I. Goldberg & Sons, Inc., found their way into Eurasia Import Co., Inc. It is possible that in a suit against I. Goldberg & Sons, Inc., and in the appointment of a receiver, an action might successfully be maintained by this receiver against Eurasia Import Co., Inc., for the return of this \$50,000 as being a fraud upon creditors. However, the amount offered in compromise is considerably in excess of this sum and we are reaching a better result than if such action was brought. While the amount offered in compromise fares badly when compared with the loss of revenue, it is apparent that this is just another case of a man in the final analysis having lost all his ill-gotten gains in the course of ordinary business. However, there will be an ultimate recovery by the Government in the sum of \$231,786.79 as follows:

Offer in compromise and refunds	\$187,786.79
Mullen forfeited bribe money	25,000.00
Homeyer fine	15,000.00
Mullen and Homeyer pension funds	<u>4,000.00</u>
Total	\$231,786.79

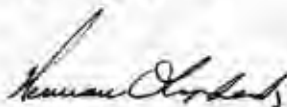
4.

The real result of the investigation and the conviction of Goldberg from a money standpoint can be seen in what the Government has saved itself by stopping the practices being committed by Goldberg. It is reasonable to presume that since the frauds had been going on for five years that they would have continued if the investigation had not taken place. A comparison of the figures for the years 1933-1934, during which the fraud was going on, and the figures of 1935-1936, which was after the investigation started, will show the preventive effect of the investigation. For the years 1933-1934 duties paid by Goldberg were \$504,747. For the years 1935 to 1936, and including only up to September 19, 1936, while the volume of importations was almost the same as the 1933-1934 period, Goldberg paid duties to the Government of \$1,258,514.00.

It is my opinion that the proposed offer is more than the Government could collect if it proceeded by action in the District Court against Goldberg, and for this reason I think that the same should be accepted. In view of the results of the appraisal of the merchandise, I believe that the inventory should be taken over by us and given to Procurement for liquidation. The offers and the various supporting documents have been prepared and have been sent to Goldberg for execution, and as soon as they are returned they will be formally submitted.

Manning is negotiating this settlement not as representative of the Treasury, but as Special Assistant Attorney General. The compromise will, therefore, have to be approved by the Attorney General.

Very truly yours,



General Counsel.

The Honorable

The Secretary of the Treasury.

Friday
February 26, 1937
4:05 p. m.

Treas.

Operator: Miss Roche is not there; her secretary has a message for you.

HMJr: All right.

T.O.: Go ahead.

HMJr: Hello -

Miss Roche's

Secy: Miss Roche asked me to give a message to Secretary Morgenthau -

HMJr: Yes

Miss R's S: She had to go over to Baltimore -

HMJr: All right.

Miss R's

Secy: - and won't be back. She expects to be at her apartment at seven-thirty.

HMJr: Well, just tell her the message on sugar is going up Monday.

Miss R's

Secy: Going up Monday?

HMJr: Yes

Miss R's

Secy: I will tell her.

HMJr: Thank you.

Miss R's

Secy: Thank you very much, sir.

HMJr: Goodbye.

Friday
February 26, 1937
4:08 p. m.

Treas.

Operator: Go ahead.

HMJr: Hello, Wayne?

W. C.

Taylor: Yes, Henry

HMJr: I thought you'd be interested to know - I think we've just been beautifully double-crossed. Wallace evidently got his message on sugar over to the President - it's going up Monday. Wallace tried to get me to bring it up in Cabinet and I wouldn't. Either he or the President brought it up, and said they were going to send it up. And then Wallace said Sumner Welles had approved of it and the Treasury hadn't done anything. So the President said, "Well, it's been around for a year." And I said, "Well, it hasn't been in the Treasury for a year." So the President said, rather crossly, "Well, it's going up Monday and if you want to do anything about it you'd better hurry." So I said, "No, Mr. President, just count the Treasury out." And I said, "We won't take any part in it one way or the other." And Ickes spoke up and he said, "Well, I haven't seen it and I'm vitally interested on account of Puerto Rico." So - he said, "I'd like to - " The President said, "Oh, don't worry, Harold, Puerto Rico's taken care of." So, my position is, we didn't - we don't know anything about it, we're not for it, we're not against it.

T: Well, when we're - when we're asked to comment on it, as we will be asked to do -

HMJr: Yes

T: I mean, see, the Chairman of that Committee will - just as a matter of form - why, send us a letter asking if we have an opinion on it.

HMJr: Well, the answer is that we weren't given an op- - we didn't have time to study it and they'll have to talk to Mr. Wallace. I'll write the letter.

T: Well, I think it's too bad. But I agree with you that that -

HMJr: Well, what are you going to do when Wallace double-crosses you?

T: I don't know.

HMJr: Yes

T: No, he - no question about it, he didn't wait on that.

HMJr: Oh no, no - Well, I'm just - I'm just going to - I'd like to ask Wallace - well, of course, he must have prepared the message for the President.

T: Oh, sure. I've got a copy of the last draft of it.

HMJr: Yes

T: - which was given me the - well, when I went over there that day.

HMJr: Yes - Well, I just thought I'd tell you.

T: Well, it's interesting.

HMJr: Well, there's just - when it goes up why we don't think about it and if we like it why I'm certainly going to - I can say anything I want about it.

T: Yes

HMJr: All right, Wayne.

T: When are you going up, tonight?

HMJr: Yes

T: You won't be coming back here then?

HMJr: No

T: Right, well, good luck to you.

HMJr: Thank you, thank you.

T: Goodbye.

Friday
February 26, 1937
4:15 p. m.

~~351~~
351

HMJr: Is that you, Dan?

Dan

Bell: Yes

HMJr:

B: Who?

HMJr: Mrs. Klotz said you wanted to talk to me? Is this Dan Bell?

B: Yes, but I - let's see, did I call you?

HMJr: I don't know.

B: I didn't call you.

HMJr: Yes - twelve twenty-one - we have a ticker system.

B: Oh - (Laughs) I guess I did. I had in here Harry Hopkins' request for money.

HMJr: Yes

B: It's only informal.

HMJr: Yes

B: With what he's already gotten in sort of driblets and what he's getting - now, he's showing some reduction -

HMJr: Hello?

Treas.

Operator: Secretary Wallace -

HMJr: Hello

Henry

Wallace: Hello

HMJr: Henry -

W: Yes

HMJr: I just want to say, you know, on that sugar tax thing -

W: Yes

HMJr: Certainly the President didn't write that message himself?

W: No, no -

HMJr: And, as far as I'm concerned, I'd much rather the Treasury wasn't asked to sit in on these things at all in the future.

W: Ah -

HMJr: Because what's the sense? -

W: Well, I'll tell you, Henry, about that. In the first place -

HMJr: Yes

W: The first draft of that went over to him, oh, quite a while ago.

HMJr: Yes

W: And he told me at that time to clear with Welles.

HMJr: Yes

W: And that was his only instruction at that time.

HMJr: Yes

W: Then later, when it came up in Cabinet meeting and you said you wanted to be in on it -

HMJr: Yes

W: Well then, we proceeded as we did.

HMJr: Yes - Well, when the bill comes down, the way I'm situated now, - I mean I've just been talking to Taylor, I mean, we're free to write any memorandum that we think is for the best financial interest of the Country and we're going to do that.

W: Yes

HMJr: And I don't know what that'll be.

W: Yes

HMJr: And I just wanted to tell you that.

W: That's perfectly all right, Henry.

HMJr: And - but I - when matters go into fifty and a hundred million dollars and you try to collect the taxes, the money just doesn't grow on trees.

W: I - I wish you'd look into it yourself with a completely open mind, however.

HMJr: But I am going to tell our people, I mean, if we can't do these things in a thorough, studious manner, I'd want - I'm not going to have our people waste their time by sitting in a committee meeting and then when the thing comes down we'll just make our independent study, that's all.

W: Yes

HMJr: And then if Congress wants to ask the opinion of the Treasury we'll give it to them.

W: The only point I want to make to you, Henry, and make it very plainly, is that - that the President had a proposed message before the matter came up in the last Cabinet meeting, that is all.

HMJr: Yes - well, I can't - I cannot be rushed and do these things in a happy-go-lucky manner and I - I'd rather not do them at all.

W: Yes

HMJr: And I haven't got enough people in the Treasury, I mean, to do these - everything in a rush. And I think the emergency is passed and I'm not going to take any more chances.

W: You know I think - I think, Henry, that in this particular matter, the reason, as I told Wayne Taylor, the last time I saw him -

HMJr: Yes

W: I think the reason the President wants to push it along -

HMJr: Yes

-4-

W: I don't know whether you were present at the last Cabinet or not.

HMJr: I was not.

W: I think it was the last one, where he indicated that he wanted to send up the crop insurance bill, he wanted to send up a tenancy bill, he wanted to - anything else - I said, "Why, yes, the sugar, - yes, I'd like to send up a sugar bill." Apparently there are a lot of things he wanted to send up that I think he felt would strengthen the - his court proposal with the farm people.

HMJr: I see.

W: I think that's really what it gets around to. He wanted to file a lot of them in. Of course, so far as sugar is concerned, there is a very real time factor on its own account, although not quite the same as the President indicated, I mean, it's - the thing doesn't expire next April. -

HMJr: Yes, well - as I say, I don't know anything about sugar and I don't know the financial aspect. And maybe when we get to it we'll be for it, I don't know. But I just didn't want any misunderstanding with you.

W: Yes - Well, I'm awfully glad you called on that.

HMJr: Yes

W: By the way, on this other matter, this housing matter, I agree with you fully that it's/as important just to bolster up the purchasing power of the - of the working population in the cities as it is the farm population; and the two are exactly one and the same thing as far as that goes. But with regard to the timing of the thing I do think that unless we do keep the purchasing power for consumers' goods steadily advancing now that there is danger of the - the so-called producers' goods getting out of step.

HMJr: Yes - but the agricultural block is going to take the position that you can't build any low-cost houses for the city.

W: Why, Henry, there's no - there's not the slightest shadow of a foundation for a statement that the agricultural block is going to take any stand like that. I have never heard any of them mention it.

HMJr: Well, I mean, I was just dumbfounded to hear you say that we should wait two years for low cost housing.

W: No, I don't think that would be quite the right way to put it. I do think that it is important that we don't have consumers' goods getting out - producers' goods getting out of line with consumers' goods.

HMJr: Well, what does that mean?

W: Why, this is what it means specifically, Henry, that - that when we say you get steel and housing and these heavy goods up beyond a certain point -

HMJr: Yes

W: - take an index over a period of fifteen years - the relationship between the consumers' goods, the things that have to do with food, the light things, you know - and the producers' goods, the heavy things; take a hundred for each of them over the period of the last fifteen years. And when the producer's good thing passes beyond the consumers' goods and stays beyond for a year, why there's trouble ahead and the thing has caught up to our step now, the first time in the last four or five years. It doesn't mean there's trouble here yet, but it does mean that the - see, what we've been pushing on, what Eccles and all the rest have been talking about ever since 1933, was to get the old - who was the old Director of the Budget? - he was also keen on that.

HMJr: Douglas is the name.

W: Douglas - our old friend Douglas - all those boys were keen on getting the producers' goods going.

HMJr: Yes

W: We picked up prosperity until we got them going.

HMJr: You mean the heavy industries?

-6-

- W: The heavy industries, yes. And they've been - they've just caught ~~step~~ now, for the first time, just the last few months, with the consumers' goods. And it means that the - just speaking in general terms, not referring to low-cost housing as contrasted with battleships, you've got battleships belonging in the same category, they're heavy industries also. I was just thinking about the thing as a whole; it's time - it's time to ease off on the heavy industry push.
- HMJr: Well, then, - -
- W: - or to put more steam into the consumers' goods.
- HMJr: Well, then, why don't they let up on road building, for instance?
- W: Yes, I think if we - I think that's a very good point, you could let up on road building, you could - or you could let up on - if we hit battleships heavily it means that you ought to do less road building, we'll say, or less bridges, at any rate, because that's more on the same style of thing.
- HMJr: Or less irrigation and building of baths.
- W: That's right, yes, I'll agree; on that side of it, Henry, I'll agree fully that - that really low-cost housing is perhaps the best type of heavy industry you can have.
- HMJr: Well, that's what shocked me so, I mean, -
- W: Well, that -
- HMJr: - to have you say, "Well, let's wait on low-cost housing for a couple of years."
- W: Well, as I - put it away in cold storage - (Laughs) but, as a matter of fact, I am glad you called because I want to get my full position before you.
- HMJr: I mean, you look over the last four years and we've done nothing for the people in the densely populated sections. Everything has been done for the people outside of the city. And we've got a very acute situation in these dense centers. And, for one reason or another, there are lots of excuses given, nothing has been done for these people, and the situation is

as acute there certainly, as it is in the share-croppers.

W: Well -

HMJr: Only they haven't got as good an advocate.

W: I'll agree with you absolutely fully, Henry, that it's as important to go in on - to help on that side as it is on the share-croppers.

HMJr: But I think, I think it's the thing, I mean, I think we ought to make a start and try to provide decent housing for these people who are living in absolutely unAmerican conditions.

W: Well, but if we do that, we should ease off on the other end - on the other end of pushing the heavy industries.

HMJr: Oh, it should come out of the five hundred million dollar pot, for Public Works, the President has -

W: Yes

HMJr: And it's just a ques- he has a five hundred million dollar pot for Public Works and he should take it out of that.

W: You will note that in the course of the discussion I did say that I thought we ought to have more of the - less of the architects - high-priced architect kind of thing and more of the really - really cheap stuff.

HMJr: Oh, in the country I don't think there is any question about it. But, the little I've studied the city housing, the important thing is to get the design correct; that's where a lot of these people have gone wrong.

W: Yes

HMJr: I mean they've had such poor designs.

W: Yes

HMJr: And when I - I mean designs and I don't mean decorations.

W: Oh, I don't - I think on that thing, Henry, if we talked it out for fifteen minutes we'd find

ourselves in very substantial accord.

HMJr: Good!

W: I -

HMJr: But, certainly, the time has come, I think, that this administration has got to recognize the slums in the densely populated sections of the cities - and possibly do a little less for the people outside of those sections.

W: Yes

HMJr: I don't say they should do any more but, I mean, I don't want to see them spend any more money, but I'd like to see it distributed a little more fairly. And especially -

W: Of course, I think - I think it's also rather important there, Henry, that we not freeze population in the wrong places, I mean, freeze them into a position of ownership in the wrong places where they can't maintain themselves.

HMJr: No, I mean, they're intelligent people, I mean that do city planning and all that sort of thing. The thing is available but it's just that they haven't been smart enough to get it across.

W: Yes

HMJr: And - I'm studying the Wagner Bill, I don't know whether it's right or wrong, but I think it's time this administration thought a little bit about the densely populated areas, except from the standpoint of social welfare.

W: Yes

HMJr: I mean, that's where your crime comes from, and diseases and everything else.

W: This matter that Madam Secretary brought up, of a shortage of labor, however, would seem to come into it to some extent, wouldn't it, if there is a shortage of the - ?

HMJr: Well, she's got some figures which, if she'll release, that just prove the opposite.

-9-

W: Is that so? (Laughs)

HMJr: Oh sure, she's got them and she's had them for two weeks.

W: Hm -

HMJr: And she hasn't released her figures.

W: Hm -

HMJr: But it's something which-I think it will go forward. It's just that these people haven't got a - haven't got the political backing, that's all. But - well, that's that. Discussions are always good and I guess everybody learns by them.

W: Well, I think it's part of the Democratic process.

HMJr: I hope so.

W: (Laughs) All right, Henry.

HMJr: All right, Henry.

W: Goodbye

HMJr: Goodbye.

TREASURY DEPARTMENT

Washington

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You doubtless recall the outstanding events which accompanied the spectacular collapse in that year. The failure of the Credit Anstalt Bank in Austria was followed, as you remember, by a run on banks in Germany which, in turn, led to a drain of gold from the Reichsbank and the Bank of England. Before the year was over England, Japan, and the Scandinavian bloc had left the gold standard and several countries had imposed exchange restrictions. By the end of 1932 six more countries had gone off gold and a half dozen others had adopted exchange controls.

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-7-

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Confronted with an acute European monetary situation that not only threatened to develop into a period of disastrous competitive depreciation but, more seriously, held grave possibilities of international political break-down, the governments of the United States, Great Britain, and France made, on September 26, 1936, an announcement which constituted a major step toward international cooperation in monetary policy.

These three governments stated, among other things, that they proposed:

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TREASURY DEPARTMENT

WASHINGTON

February 27, 1937.

MEMORANDUM FOR THE SECRETARY:

The following telegram has been received from the West Coast, with further reference to the Lew Kim Yuen case:

"Teletype information Portland Lew Kim Yuen failed to appear in court to-day and bond five thousand dollars ordered forfeited by Judge Fee. Bench warrant issued. Every effort being made to apprehend Lew Kim Yuen who has been indicted with others on conspiracy to violate narcotic import and export act. Bail fixed by court for Lew Kim Yuen Twenty-five thousand dollars on secret indictment returned February twentieth."

Needless to say, every effort will be made to apprehend this fugitive.

GRAVES.

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Confronted with an acute European monetary situation that not only threatened to develop into a period of disastrous competitive depreciation but, more seriously, held grave possibilities of international political break-down, the governments of the United States, Great Britain, and France made, on September 26, 1936, an announcement which constituted a major step toward international cooperation in monetary policy.

These three governments stated, among other things, that they proposed:

Taking into full account the requirements of internal prosperity, to maintain the greatest possible equilibrium in the system of international exchange and to avoid to the utmost extent the creation of any disturbances of that system by internal monetary action.

The three governments invited the cooperation of other nations to realize the policy laid down in the declaration.

To further implement this statement, the Secretary of the Treasury announced, on October 14th, that gold would be sold to the exchange equalization or stabilization funds of those countries whose funds likewise were offering to sell gold to the United States on terms advantageous to the United States.

France and Great Britain were named as complying with the conditions, for the purchase of gold from the United States.

On November 24, 1936, Belgium, the Netherlands, and Switzerland indicated their adherence to the principles contained in the tripartite announcement, and these countries were added to the list of countries to which the United States would sell gold.

VII. TO PROTECT THE DOMESTIC ECONOMY FROM EFFECTS OF ABNORMAL INTERNATIONAL GOLD MOVEMENTS THE TREASURY, ON DECEMBER 24, 1936, BEGAN A POLICY OF "STERILIZING" GOLD ACQUISITIONS WHENEVER CONDITIONS JUSTIFY.

To date about 190 million dollars worth of gold has been placed in the inactive account.

this comes perhaps
just before final
draft

385

*This has some
change*

386

I. WHAT ARE THE GOALS OF MONETARY POLICY?

A. In the domestic field our goals are:

(1) To attain, and once attained to maintain, reasonably equitable and stable income relationships among the different groups: workers, farmers, business men, investors, etc.

(2) To prevent marked fluctuations or sharp trends in wholesale price levels.

(3) To maintain a moderately stable cost of living.

(4) To foster steadily increasing employment and an orderly expansion of business activity.

B. In the international field our goals are:

(1) To maintain that position of the dollar with reference to other currencies that will encourage an increasing domestic and foreign trade, and thereby help promote peace.

(2) To eliminate broad fluctuations in exchange rates without sacrificing sovereignty over our monetary policy.

(3) To facilitate the smooth and easy adjustment of international payments and foster stability of foreign monetary systems.

(4) To avoid competitive depreciation of currencies.

II. THESE ARE THE OBJECTIVES. THEY ARE NOT TO BE EASILY OR QUICKLY ATTAINED. WE ARE NOT EVEN CERTAIN THEY CAN BE CLOSELY APPROACHED.

Whatever its merits in theory, the old pattern of monetary system, with its presumed reliance on automatic operation, can hardly be said to have promoted the foregoing objectives. The new pattern which is evolving places its emphasis on "control" or "management". We do not yet know exactly the final pattern that will emerge. Whether it will prove better able to approach the goals I have just mentioned remains to be seen. We think it will.

III. IN DEVELOPING THE NEW PATTERN WE HAVE TO
FEEL OUR WAY CAREFULLY.

We are, in a sense, in uncharted seas, and we must proceed cautiously; we have to test and verify each step, and go only so fast as we can see clearly ahead.

The numerous monetary measures and regulations adopted in the past four years, though designed to meet problems as they arise, are not a collection of haphazard devices. They fit into a pattern, into a sequence that -- with possibly one exception -- is leading us in the direction of the objectives I enumerated above.

I am sure that the monetary changes that have occurred are familiar to you. Nevertheless, a brief resumé of the evolution of the new pattern as it appears to one who has participated in its actual formulation and is responsible for its practical administration may be of interest. In any case, it will provide a good starting point for the discussion.

IV. THE OLD PATTERN, PATCHED UP AFTER THE WAR,
BROKE DOWN UNDER THE IMPACT OF THE DEPRESSION.

Just when it began to weaken is difficult to say.

The crumbling became apparent to most observers in 1931.

You doubtless recall the outstanding events which accompanied the spectacular collapse in that year. The failure of the Credit Anstalt Bank in Austria was followed, as you remember, by a run on banks in Germany which, in turn, led to a drain of gold from the Reichsbank and the Bank of England. Before the year was over England, Japan, and the Scandinavian bloc left the gold standard and several countries had imposed exchange restrictions. By the end of 1932 six more countries went off gold and a half dozen others adopted exchange controls.

Only France, Switzerland, Netherlands, Belgium, and

- 5 -

the United States clung to the gold standard. In March 1933 we joined the process of those countries who were determined to begin the process of recovery with the aid of a new monetary pattern.

V. IN MARCH 1933 THE UNITED STATES BROKE AWAY FROM THE SHACKLES OF THE OLD ORDER AND THE NEW PATTERN BEGAN TO EMERGE.

The first step was for the Government to take control of internal gold holdings.

(1) On March 6 the banks and Government offices were prohibited by Presidential proclamation from paying out gold. The increase in gold hoarding was thus immediately stopped.

(2) On April 5 an Executive Order required gold and gold certificates to be surrendered. Internal hoards of gold were given up, and thus complete control of all monetary gold in the United States was achieved.

- 6 -

(3) On June 5 Congress declared "gold clauses" invalid, thereby severing internal monetary transactions from the international monetary standard.

The second and overlapping step was for the Government to take control of the external flow of gold.

(1) On March 6 and 10, Executive Orders were issued prohibiting the export of gold except under regulations or licenses.

(2) On April 20 an Executive Order defined the authority of the Secretary of the Treasury to issue licenses to export or earmark gold, for transactions in foreign exchange, transfers of credit, and exports of currency and coin.

THE UNITED STATES GOVERNMENT WAS THEN IN A POSITION TO DECLARE TO THE WORLD ITS MONETARY INDEPENDENCE.

While the World Economic Conference was in session

in London waiting hungrily for the United States to graciously distribute largesse in the form of generous debt remissions, additional credits, tariff reductions, an over-valuation of the dollar, and a return to the fetters of the automatic gold standard, the President sent a message which unequivocally stated our new monetary objectives.

I can do no better than quote from that historic message:

"..... old fetishes of so-called international bankers are being replaced by efforts to plan national currencies with the objective of giving to those currencies a continuing purchasing power which does not greatly vary in terms of the commodities and need of modern civilization. Let me be frank in saying that the United States seeks the kind of a dollar which a generation hence will have the

- 8 -

same purchasing and debt paying power as the dollar value we hope to attain in the near future. That objective means more to the good of other nations than a fixed ratio for a month or two in terms of the pound or franc. Our broad purpose is the permanent stabilization of every nation's currency."

THE GOVERNMENT WAS NOT CONFRONTED WITH THE TASK OF DEVELOPING A MECHANISM OF CONTROL TO GIVE EFFECT TO OUR NEW POLICY.

(1) On August 29 sales to industry and abroad of newly-mined domestic gold were authorized by Executive Order.

(2) On October 25 the Reconstruction Finance Corporation was authorized by Executive Order to acquire newly-mined domestic gold. The rate at which gold was purchased was announced from time to time, and varied from \$29.00 to \$34.45 per ounce during the period of purchases.

- 9 -

(3) On January 30, 1934, the Gold Reserve Act amplified and consolidated the essential instruments of control.

(a) Title to all gold of the Federal Reserve

System was transferred to the United States.

(b) The weight of the gold dollar was not to be

fixed at more than 60 percent of its existing

weight. The Farm Relief Act, passed in the

previous year, had already placed the lower limit

at not less than 50 percent.

(c) A Stabilization Fund of two billion dollars

was established.

(d) The authority of the Secretary of the Treasury

to buy and sell gold at such rates and upon

such terms as he may deem most advantageous to

the public interest was reaffirmed.

(4) On January 31, 1934, the weight of the gold dollar

- 10 -

was fixed by Proclamation of the President at 15-5/21 grains of gold 9/10th fine. On the same day purchase of gold was authorized at \$35 per ounce, less 1/4th of one percent, and it was announced that gold would be sold for export to foreign central banks whenever our exchange rates with gold standard currencies reached gold export points.

THE PERIOD OF ACTIVE INTERNATIONAL COOPERATION
BEGAN WITH THE TRIPARTITE ACCORD.

Confronted with an acute European monetary situation that not only threatened to develop into a period of disastrous competitive depreciation but, more seriously, held grave possibilities of international political breakdown, the governments of the United States, Great Britain, and France concluded, on September 26, 1936, an accord which constituted a major step toward international cooperation in monetary policy.

- 11 -

These three governments stated, among other things, that:

Taking into full account the requirements of internal prosperity, to maintain the greatest possible equilibrium in the system of international exchange and to avoid to the utmost extent the creation of any disturbances of that system by internal monetary action.

The three governments invited the cooperation of other nations to realize the policy laid down in the declaration.

To further implement this accord, the Secretary of the Treasury announced, on October 14th, that gold would be sold to the exchange equalization or stabilization funds of those countries whose funds likewise are offering to sell gold to the United States.

France and Great Britain were named as complying with

the conditions, for the purchase of gold from the United States.

On November 24, 1936, Belgium, the Netherlands, and Switzerland indicated their adherence to the principles contained in the tripartite accord, and these countries were added to the list of countries to which the United States would sell or export gold.

VII. TO PROTECT THE DOMESTIC ECONOMY FROM EFFECTS OF ABNORMAL INTERNATIONAL GOLD MOVEMENTS THE TREASURY, ON DECEMBER 24, 1936, BEGAN ITS POLICY OF "STERILIZING" GOLD ACQUISITIONS.

To date about 190 million dollars worth of gold have been placed in the inactive account.

This brief outline presents an interpretation of the measures we have adopted in pursuit of the objectives I outlined earlier.

The Government Security Market

Week ended February 27, 1937

- - * - -

The general level of the market for Treasury bonds at the close of the past week was about the same as it was at the beginning of the week. The Secretary's announcement on the March 15th financing Thursday resulted in a good demand and price advances on that day about offset irregularly lower prices on the other four trading days. Volume continued to be small and trading was altogether in small lots with the long maturities still in the best demand. However, short and intermediate maturities were steadier than for some time and day-to-day price changes for these were confined to small fractions. Net changes for the week show gains of 1 to 3/32nds by the three longest maturities while all other issues were generally unchanged to 2/32nds lower. In the average, Guaranteed issues finished 1/32nd lower.

In the Treasury note market the April "rights" advanced to 101.6 bid on Thursday but subsequently eased to close at 101.3 bid, up 2/32nds. At this price the current premium placed on the rights is about 3/4s of a point. There was a small amount of selling in the long notes and this, with a fair amount of switching out of them, resulted in losses of 3 to 6/32nds by those issues maturing after June 15, 1939. In the short issues the September 1937 maturity advanced 1/32nd, while all others lost 1/32nd.

J. M. Harris

ms. 1107. A
Please these
Read this cable,
tell them to continue sending
kind of cables. H.M.F.

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Tokyo, Japan

DATE: February 27, 1937, 6 p.m.

NO.: 64

Reference is made to telegram No. 59 of February 19, 5 p.m., paragraph three, from the Embassy.

FOR THE SECRETARY OF THE TREASURY.

First. A report was recently published in the Japanese press that the Government intended to ship gold from the specie reserve to the United States in early March to the value of 10 million yen. It was stated that throughout the year it intended to ship newly mined gold purchased by the Government either to London or New York. It was estimated that the total shipments during the year would probably amount to 130 million yen at the present exchange value of the yen.

Second. The Commercial Attaché of the Embassy was informed this morning by Tsushima that the above report is a newspaper fabrication. Tsushima said that the Government as yet has made no definite plans as to the times, destinations or amounts of any shipments of gold they may make. He particularly wanted it to be known that the shipments when and if made need ^{not} be a cause for uneasiness as to the specie reserve of Japan, as at present this reserve is excessive. Eventually, he ^{indicated} ~~said~~, Japan does intend to ship gold to the United States, because he asked the Commercial Attache if he thought which gold ship-

- 2 -

ments would interfere with the policy of the Treasury of discouraging heavy influx of gold into the United States. The reply of the Commercial Attaché was that he did not think there would be any trouble from small shipments.

Third. We assume that Secretary Morgenthau wants us to continue telegraphic reports at intervals on important fiscal developments in Japan; please instruct if this assumption is not correct.

GREW.

EA:LWW

RECEIVED
JAN 24 1931
U.S. DEPARTMENT OF THE TREASURY

JAN 24 1931

RECEIVED

WORKS PROGRESS ADMINISTRATION

WALKER-JOHNSON BUILDING
1734 NEW YORK AVENUE NW.
WASHINGTON, D. C.

HARRY L. HOPKINS
ADMINISTRATOR

February 27, 1937

Dear Henry:

You will recall that sometime ago I said we hoped to get 25,000 non-relief and administrative employees transferred out of the WPA prior to January 1. I am enclosing copy of the record on that. It shows that we dropped 6,000 administrative employees from August 31 to January 31, and nearly 29,000 non-relief workers during the same period. I am convinced this will show a further drop in the months of February and March, respectively.

Very sincerely yours,



Administrator.

The Secretary,
The Treasury Department,
Washington, D.C.

Encl

WORKS PROGRESS ADMINISTRATION

Number of Administrative and Non-Relief
Employees by Months

August 1936 -- January 1937

<u>MONTH</u>	<u>STATES</u>	<u>CENTRAL OFFICE</u>	<u>TOTAL</u>	<u>NON-RELIEF</u>	<u>GRAND TOTAL</u>
August	34,189	2,381	36,570	122,924	159,494
September	33,518	2,272	35,790	126,974	162,764
October	33,271	2,162	35,433	131,276	166,709
November	32,071	2,139	34,210	130,393	164,603
December	29,445	2,023	31,468	116,689	148,157
January	28,522	2,011	30,533	100,379	130,912

Feb. 20, 1937

BK 56
403

MM

~~MM~~

GRAY

PARIS

Dated Feb. 27, 1937

Rec'd. 10:10am.

Secretary of State

Washington, D.C.

284, February 27, noon. (SECTION ONE).

In the debate on general policy which took place yesterday afternoon and last night in the Chamber, the Government received a vote of confidence with its customary majority of approximately 150 votes.

The financial aspects of the debate will be reported in detail in Cochran's telegram for the Treasury. For background purposes you may be interested in the following: there has for some time been a growing uneasiness regarding Government finances and the problem of rapidly rising costs. Speaking two weeks ago to Government employees who were demanding salary increases Blum stated the necessity of a "pause" as regards the realization of the Government's social and economic program. He repeated this warning the following day to the National Council of the Socialist Party. Flandin thereupon announced his intention of interpellating the Government as to the exact significance of the "pause" stating that he felt a matter involving the economic program of the Government was of such importance that it should be debated before the Chamber and a full explanation given. (END SECTION ONE).

WILSON

U

GRAY

Paris

Dated February 27, 1937

Rec'd 11:40 a.m.

Secretary of State

Washington

284, February 27, noon (SECTION TWO)

by Blum as to what he had in mind. At this time indications appeared that Blum was perhaps considering a modification of policy in an effort to restore confidence involving among other things the replacement of the Minister of Finance and of the Governor of the Bank of France. Whatever foundation there may have been at one time for the reports that these changes were under consideration Blum's speech at St. Nazaire and Nantes a week ago made it clear that he had definitely decided against any modification of the Government's program or any changes in the personnel of his Government. He also made it clear in these speeches that the "pause" meant merely factional breathing spell to consolidate the gains already made in the economic and social field whereupon the Government would resume measures to realize its full program. In other words, in these speeches at St. Nazaire and Nantes, Blum effectively answered in advance Flaudin's interpellation.

Apart from the purely financial aspects the debate
yesterday

U -2- #284, Feb. 27, noon (SEC. 2) from Paris

yesterday was of interest in that it drew from Blum the statement that after the "pause" the program which the Government intends to complete is the program approved by all the parties concerned composing the Popular Front and that any extension of this program would require similar approval by these parties, including the Radical Socialists. This statement would seem to be a disavowal of recent speeches by Jouhaux, Faure and Thorez announcing an advanced Socialist program including "nationalization" of banks and insurance companies.

WILSON

HPD

PARAPHRASE OF SECTION THREE. No. 284 of February 27, 1937, from PARIS.

CONFIDENTIAL.

The position of the Radical Socialists is difficult at present. A meeting was held by the parliamentary group of the Radical Socialist Party on the day before the Chamber debate in which the financial and economic policies of the Government were severely criticized. Decision was reached by the party, however, to vote in favor of the Government. This was not so much - according to some Party members - because they had confidence in the Government, but at this time they did not want to assume the responsibility of overthrowing the Government. They preferred to let the Government bring about its own downfall.

I had a conversation with one of the leaders of the Radical Socialist Party. He was outspoken in his condemnation of the financial and economic policies of the Government. All that would be needed for restoration of the necessary confidence he said would be for Blum to discard the Communists, make two or three Cabinet changes, and make reductions in governmental expenditures for the time being at least. However, Blum was ^{either} not willing to do these things because of doctrinal reasons, or he was not able to do them because of past political commitments. My informant said that under these circumstances he saw no solution and that the country was moving towards an inevitable financial crisis.

Yesterday

- 2 -

Yesterday while Blum was speaking in the Chamber I was present. I was interested in observing that an important fraction of the Radical Socialists refrained from any applause or indication of approval of the statements made by Blum.

END MESSAGE.

WILSON.

EA:LWW

RECEIVED
TREASURY DEPARTMENT
Office of the Secretary
Treasury Building, Washington, D.C.

BK 56
408 M

MM

GRAY

PARIS

Dated Feb. 27, 1937

Rec'd. 11:50am.

Secretary of State
Washington, D.C.

286, February 27, 1pm. (SECTION ONE).
FROM COCHERAN.

The debate last evening in the Chamber of Deputies on the financial and economic policy of the Government ended in a vote of confidence of 360 to 209 following the interpellation by Flandin on the general policy of the administration and severe criticism by Reynaud who warned the Government notably that its policy risked to isolate France economically and financially from the United States and Great Britain.

At the outset of his interpellation Flandin referred to recent declarations of Blum and rumors circulated of nomination of a new Governor of the Bank of France, a new Minister of Finance and an extension of the Government's majority towards center. He thought it was high time to enlighten public opinion in this respect and also as to what was meant by the "pause" announced by Blum. As to the latter, Jouhaux had stated that immediately after the opening of the Paris Exposition the Government should proceed with the execution of the plan of the general confederation of labor. Flandin thought this might really be the situation as Communist leader Thorez had said that

mm 286, Feb. 27, 1931. Section One, from Paris -2-

that the Socialist defined Communist parties unity of action pact would at that time have ended in a united labor party headed by Blum. The Chamber and the country awaited a denial or confirmation in this respect. Flandin pointed out that the Popular Front program in effect seemed to have been realized save the national employment fund, assurance against agriculture disasters and old age pensions.

Flandin then developed his interpellation as follows.
(END SECTION ONE).

WILSON

KLP

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GRAY

PARIS

Dated Feb. 27, 1937

Rec'd. 11:55am.

Secretary of State

Washington, D.C.

286, February 27, 1pm. (SECTION TWO).

Blum had carried out his program in such a way as to dissipate any doubts as to present or future. He had announced that it only represented a step "designed to facilitate the putting into practice and the success of the Socialist program". The "pause" was to prepare the country for this new step.

The debate was of a grave and serious character but he (Flandin) had persisted in raising it in spite of advice of certain friends "to refrain until events would precipitate it", such as the announcement of an empty treasury, a request for additional advances from the Bank of France, or the publication of a statement of the latter showing gold losses.

The Government claimed that not only would it avoid a catastrophe but "would lead democracy to a magnificent future". However, Flandin and his friends were convinced that Blum "was leading the country to a catastrophe and that the Republican regime would perish if Blum persisted in following his present policy". (END SECTION TWO)

WILSON

RB

GRAY

Paris

Dated February 27, 1937

Rec'd 12:10 p. m.

Secretary of State
Washington.

286, February 27, 1 p. m. (SECTION THREE).

Flandin predicted that events would not permit delay in deciding upon future policy. The financial and monetary situation would make this impossible. The Treasury was in a serious situation and this was known to all. Government employees were not being paid and he was reliably informed that orders had gone out to the different ministries to halt expenditures. Furthermore the Government was trying to arrange another loan abroad.

No Government had ever possessed such large authorizations to borrow. The Government had a margin of issue of Treasury bonds but what was serious was that they could not find any takers. The Government had never tried to issue a long term loan although this type of loan appealed to the small man who the Government claimed had confidence in the Popular Front. 25% of holders of "Oriol" bonds had refused to renew them in spite of premium offered of forty per cent.

RB

-2- 286, February 27, 1 p. m. from
Paris

per cent. Subscriptions in gold to the "national defense" loan only amounted to one hundred and seventy-two million francs gold according to Oriol's own statement to the Finance Committee. Although the rate of interest on Treasury bonds had been raised to $3 \frac{7}{8} \%$ the Treasury could only place the total with difficulty if at all.

Furthermore, it was public knowledge that two large British banks had refused to participate in recent British credit in spite of gold guarantee. While all other currencies which had been devaluated were sought on the London market the franc was not. Did the Government contend that a "money bloc" existed in London against the franc?

WILSON

HPD

RB

GRAY

Paris

Dated February 27, 1937

Rec'd 12:20 p. m.

Secretary of State
Washington.

286, February 27, 1 p. m. (SECTION FOUR).

Blum had claimed improvement in savings accounts but this had always been the case in January. Furthermore, since May 1936 savings had decreased by four billion francs. Devaluation and higher prices accounted for the increase in tax revenue. Increase in railway revenue was due chiefly to transport of British coal imported. Even if railway revenue increased during 1937 by 1 and 1/2 billions Blum had himself stated that 40 hour law would increase expenditures by 1,800,000,000.

Therefore under present conditions no improvement in treasury or railways could be hoped for. On the contrary prospects were for an opposite result. Unemployment costs were far above estimates, the general rise of prices would automatically lead to revision of contracts passed with public administrations. Increase of pay of civil servants was inevitable.

— Increased

RB

-2-1286, February 27, 1 p. m. from
Paris (SECTION FOUR)

Increased buying power was basis of government's policy but increased prices would "absorb or freeze" capital which could be thus made available for Treasury.

Deposits in the banks in spite of devaluation have been increased. The country was not in a condition to provide the money necessary for the Treasury in 1937. The Government would soon have to have direct or indirect recourse to the Bank of France to meet Treasury outlays.

If Government counted upon profit from devaluation to minimum of 43 milligram a new convention would be
(END SECTION FOUR)

WILSON

WWC

PARIS

Dated Feb. 27, 1937.

Recd 1:45 p.m.

Secretary of State,
Washington.

286, February 27, 1 p.m. (SECTION FIVE)

necessary with the Bank of France (to this Auriol said he would not reply.)

The monetary situation was as serious as the financial situation. The exchange fund had on January 29 exhausted its gold at the bank resulting from revaluation of the gold reserves. It was true that the fund could continue to take gold from bank but this would diminish gold reserves of latter.

Under such circumstances the uneasiness about the franc would be substantially increased especially as the public had been assured that franc at new parity after devaluation, "was in fact guaranteed by the tripartite arrangement which I do not believe is exact." Uneasiness about franc was reflected in forward rates of dollar and pound. Lack of confidence future of franc was due to psychological reasons and it would be erroneous to claim otherwise. Speculation should not be blamed. Very real reasons existed, such, for instance, as deficit in ever increasing commercial balance. Exports should benefit by devaluation but domestic prices already exceeded world prices.

CA --2--Paris 286 Feb 27, Sec 5....

prices. Raw materials necessary for France will continue to increase commercial deficit.

If Government fights price increase by manipulating customs, tariffs and quotas, the deficit will be aggravated as it will lead to increase of imports of foreign merchandise. The influx of visitors counted on may not come up to expectations. Even if there are 2,000,000 visitors and each leaves 2,000 francs, the 4,000,000,000 francs thus recuperated will be less than required to repay British credit in November next.

WILSON

SMS NPL

RB

GRAY

Paris

Dated February 27, 1937

Rec'd 12:35 p. m.

Secretary of State

Washington.

286, February 27, 1 p. m. (SECTION SIX)

Events are leading up to an almost simultaneous monetary and Treasury crisis. The only method of financing requirements will be by inflation and defense of the franc by exchange control although the Government has solemnly repudiated intentions. However, it would have no choice.

A way out was offered by a return to a real liberty of movement of capital within the framework of a general policy of price, liberty and social order.

He, Flandin, had at one moment thought Blum intended to adopt such a policy especially in connection with Blum's search for peace guarantees in Europe and elsewhere. But if the Government established exchange control it would "alienate the cooperation of the two democracies upon whose support you have based guarantees of peace". Flandin continued; "I am not sure, but I think I can guess the undertakings you have entered into in this respect with London and with Washington".

If the Government wishes to restore confidence and

induce

RB

-2-286, February 27, 1 p. m. from
Paris (SECTION SIX)

induce the return of French and foreign capital it must
urge union, and it must cease, above all systematically to
oppose capital and labor, as if the one without the other
were not totally powerless. (END SECTION SIX)

WILSON

KLP

PARIS

Dated Feb. 27, 1937.

Recd 1:50 p.m.

Secretary of State,
Washington.

286, February 27, 1 p.m. (SECTION SEVEN)

The advisers of the Government imprudently proclaimed without ceasing that revolution would soon crush capitalism. While Jouhaux announced a great program of nationalization of credit, of insurance of railways and the key industries, Minister Faure called for consolidations and mobilization of fortunes. Severac stressed that the role of the Socialists was to demolish the regime of capitalism, and Communist Thorez announced a few days ago that it was possible to set up the Soviet regime in France at an early date and claimed that he would soon be at the head of the country.

Addressing Blum, Flandin asked the Premier how he could allow such language by his Ministers; if they did not interpret Blum's own thoughts, Flandin doubted that Blum's explanation of the announced "pause" could restore domestic and international confidence and that he would finally be induced by his "entourage" to proceed to constraint. Such methods he predicted would not be specifically Socialist. They would smack of Hitler and Mussolini, not to speak of Lenin, and Stalin.

Turning to Blum's satisfaction at his formation of
the "block of

CA --2---206 Paris Feb 27 Sec 7...

"block of democracies in opposition to totalitarianism states" Flandin stressed view "that the United States and Great Britain would feel some repulsion for Stalinian totalitarianism."

END SECTION SEVEN.

WILSON.

SIS NPL

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GRAY

Paris

Dated February 27, 1937

Rec'd 2 p. m.

Secretary of State
Washington.

286, February 27, 1 p. m. (SECTION EIGHT)

Flandin was followed at the Tribune by Fernand Laurent who invited attention to the serious outward movement of gold, "at the rate of one billion francs" weekly and quoted LONDON TIMES that between last week of January and February 15 about twenty-three and a half million pounds had gone to England, from February 18 to 22, four million pounds and daily since February 22 at the average rate of two hundred million francs daily. Auriol interrupted to say this was inexact and claimed that figures had been furnished Fernand Laurent "by a high official of the Bank of France". Auriol protested that the exchange fund operations were secret. He repeated, however, that the Deputy's information was false.

The situation had improved during the last few days, Auriol claimed, and he refused to admit a request for a commission of inquiry. At this point the debate became

confused

RB

-2-#286, February 27, 1 p. m. from
Paris (SECTION EIGHT)

confused and assertions were made that the Government in reality represented Moscow. Fernand Laurent denied that he had been in communication with an official of the bank.

Fernand Laurent recalled that Flandin had warned the Government that it must change its policy before May, but the Government well knew that an immediate change was imperative if the financial and economic situation was to be saved. Technical remedies in his view could not save the day. The remedy was political, "by an immediate and profound psychological shock". He pointed to the collapse of prices on the Bourse which followed Blum's speech at St. Nazaire indicating that he would not change his policy. He quoted statistics to show that the economic situation had not in reality improved, save for certain industries engaged in supplying armaments and that the reduction in

WILSON

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GRAY.

Paris

Dated February 27, 1937

Rec'd 5:00 p.m.

Secretary of State,
Washington.

236, February 27, 1 p.m. SECTION NINE

unemployment was due to the new army service law.

Reynaud dwelt notably on the failure of the policy of increased purchasing power and insisted that the decision to "pause" was the proof. The financial problem, in his view, was secondary. The trouble was internal and profound. Reynaud pointed out that in payment of the large quantities of raw material imported, the foreign supplier had the choice of two methods of payment. If French merchandise was cheaper than gold, he took French merchandise, but if gold was cheaper, that it to say if it had greater purchasing power abroad, he took ^{gold} in payment. This was in substance the whole problem. If merchandise was too dear and on the other hand it was imperative to hold gold on account of national defense requirements, dictatorial methods remained. But if those were resorted

sms 2 - No. 286, February 27 from Paris. Section 9 resorted to, the patrimony of France would be wasted in a few months. Therefore, it was only by French labor that France could pay for its imports.

Reynaud then proceeded to refer to the tripartite monetary agreement which he recalled that he had favored and regarded as being important. In principle it supposed that the three democracies would follow a policy of peace. He then said textually:

"I know all that might be said about the intimate sentiment of the mass of Americans as concerns distance from Europe; but it is extremely (#) on a document which bears the signature of these three countries that they declared themselves in agreement to follow three purposes, namely, to

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(#) Apparent Omission

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GRAY

Paris

Dated February 27, 1937

Rec'd 2:10 p.m.

Secretary of State
Washington.

286, February 27, 1 p.m. SECTION TEN

safeguard peace, to favor the establishment of conditions that would best contribute to restore order in international economic relations, and to follow a policy tending to develop prosperity in the world and to improve the level of living of peoples."

Nothing better could be said, he continued, and in carrying out these written words the French Government had given undertakings. It had undertaken to follow a certain policy and here he quoted the document. France was bound by these provisions and he could not imagine that any French Government would take the responsibility of destroying the arrangement signed by Blum. He (#) that when Blum said at St. Nazaire that he intended to act with respect to prices, to extend quotas, and to facilitate the entry of merchandise into France that he had this in mind.

Reynaud

RB 2- No. 286, February 27 from Paris, Section 10

Reynaud was not sure^{if}/it was not too late to do this. Devaluation should have been followed with reduction of French prices to level of world prices so that quotas could have been suppressed without danger to French economy. Today prices abroad were rising and the opportunity would have been magnificent for France to recover its economic equilibrium. The pity of it all was that the opportunity had been lost and today there was a debtor balance.

Neither the monetary system nor the budget mattered if the ensemble of the Government's policy did not reestablish the economic equilibrium of France.

As it was, French producers demanded the strengthening of customs barriers although today customs protection

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Paris

Dated February 27, 1937

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236, February 27, 1 p.m. SECTION ELEVEN

was higher than on the eve of devaluation. What had happened was that the Government had suppressed several hundred quotas which "were already useless" and then reduced tariffs by twenty percent. An article purchased in England before devaluation at a cost of ninety-five francs now cost one hundred and twenty-one francs, and yet French producers still demanded higher protection in order to continue to do business.

Abroad France was regarded as hesitating between the liberalism of democracies and the closed economy of dictatorships and the LONDON TIMES had just emphasized that France would soon find itself once more isolated economically unless it changed Government policy.

Reynaud noted that already bankers had received oral instruction to take steps to reduce purchases of foreign currencies by individuals in spite of recent

categorie

sms 2 - No. 286, February 27, from Paris. Section 11
categorical declaration of the Minister of Finance.
Exchange control would hinder the outflow of capital
to a small extent but it would radically halt the
inflow and this would be absurd in view of the fact
that "the cage veers".

Therefore, there were two policies. On the one
hand, the tripartite agreement, and, on the other hand,
the policy of high prices. The "pause" could not
possibly stop the inevitable consequences of such a
contradiction.

Blum, in the name of the Minister of Finance,
then briefly replied by a somewhat disconnected reminder
of efforts already made to reorganize departmental
and communal expenditures, explanation regarding a
complaint that the

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Paris

Dated February 27, 1937

Rec'd 5:15 p.m.

Secretary of State,
Washington.

206, February 27, 1 p.m. SECTION TWELVE
Government was responsible for limiting the employment of labor on the Exposition to members of the Confederation of Labor. Flandin had said that the Government was leading the country to a catastrophe and Reynaud had said the country was being led to ruin. However, neither had pointed the way to salvation.

Blum, however, confined himself almost entirely to stating that the origin of the Government, the work it had accomplished, and its repeated declarations provided Government's reply. When he had spoken of a "pause" he did not by any means intend to make a gesture of contrition and he did not intend to recognize as justified the bitter criticism of the administration made by Flandin. He would not admit that the Government had failed, on the contrary, "he and his ministers had the right to affirm that the situation today was better."

The

sms 2 - No. 286, February 27, from Paris. Section 12

The country was gradually recovering economically. It would not be difficult for him to refute figures quoted to the contrary.

Blum insisted that unemployment had receded and that savings were increasing. If it is true that British coal transport had increased railways earnings, it showed that industry was more active. If gold exports were considerable, they were also substantial when Flandin and Laval were in office. No one could deny that an improvement had taken place in the country. This was obvious by a walk through Paris or the ^(country?) contrary. The transformation was perhaps more moral than material "as people had recovered confidence in themselves".

He meant by the "pause" that "during a certain time it was necessary to introduce into the Government's program a certain spirit of prudence and care that the rhythm

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Paris

Dated February 27, 1937

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286, February 27, 1 p.m.. SECTION THIRTEEN
should be slowed up and that perhaps certain measures
they had in mind should be deferred."

As to prices, he was less preoccupied with the
export prices than with domestic prices. He was con-
vinced that in many cases prices reflected too much
greed. While social reforms had undoubtedly affected
prices, these reforms could not have been put off as
the social danger was too great.

Treasury difficulties would not cease until
exported and hoarded funds had been returned to cir-
culation. Public credit and private economy needed a
relatively tranquil breathing spell to recover. He
believed that these explanations were clear and logical.
While they were not as short as he might have desired,
he could not say less without lack of respect for his
interpellators and the Chamber itself.

As to

sms 2 - No. 286, February 27, from Paris. Section 13

As to the political side of the debate and the question of future policy, the pause would not interrupt the "symphony". The Government's policy would be resumed when circumstances permitted. (?) future as concerned the Government the reply was simple:

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GRAY

Paris

Dated February 27, 1937

Rec'd 5:30 p.m.

Secretary of State,
Washington.

286, February 27, 1 p.m. SECTION FOURTEEN

"The Government would proceed to the same ends towards the achievement of the ministerial program which was the program of the Popular Front. Furthermore, they would not leave this program completely suspended. The Chamber would not be sent on a vacation. The Senate had before it the law on the trade and on the amnesty, and the Chamber would pursue the discussion of the agricultural laws, and the national unemployment fund project would follow soon.

After the pause the Government would take up the reforms embodied in the Popular Front program but as concerns necessary outlays they would take into consideration the present state of economy and public credit.

They had no reason whatever to change their purpose and this purpose was that of the Popular Front. This
program

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sms 2 - No. 286, February 27, from Paris. Section 14
program was the only one in regard to which an under-
taking existed between parties. It was the only one to
which the majority was tied to vis-a-vis the country.
It was the only one to which the Government was tied
to as concerned the majority."

Blum definitely stated that he had no intention
of transforming the Popular Front Government into a
National Government and that he had no intention of
withdrawing. He visualized the perils to the demo-
cratic institutions of France if the present adminis-
tration should fall.

END OF MESSAGE

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PARIS

Dated Feb. 27, 1937.

Recd 5 :20 p;m.

Secretary of State,
Washington.

285, February 27, 1 p.m. FROM COCHRAN

In commenting editorially upon Chamber debate of last night the AGENCE ECONOMIQUE ET FINANCIERE says this did nothing to clarify the important problem, that is as to who is going to put France back into the big circle of world recovery. This paper considered that the Prime Minister was adroit in handling the political side of the situation but failed to give any indication of measures toward lifting the restraint now holding back French recovery. The editor of the LA JOURNEE INDUSTRIELLE says doubts are becoming more general as to merits of the Government's policies. He hints that present political strategy may lead to a new push toward a Marxist dictatorship. British financial press this morning give detailed account of debate stressing severity of attack on the Government. It is too early for editorial comment. Unofficial exchange trading this forenoon revealed sharp uneasiness caused by Blum's attitude in last night's

(END SECTION ONE.)

WILSON

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PARAPHRASE (PARTIAL) OF SECTION TWO, No. 285
from Paris.

debate. There was a fairly good demand for dollars and Bank of France is said to have yielded important amount of sterling. Some big Paris banks which wanted sterling but hesitated to apply therefore at Bank of France endeavored to get a Paris American bank to buy for them. Forward franc more offered. Other European curbings stronger against the franc.

Press reports from Stockholm that at annual meeting of Svenska Handels Banken the Managing Director strongly warned against idea of increasing value of crown in relation to the sterling.

(?) Weil yesterday invoiced Baker and Company 487,000 francs; bar silver, and Comptoir Lyonnais and to Guaranty 1,230,000 francs gold bars both ILE DE FRANCE. I believe gold shipment represented proceeds of gold coins exported from Germany for refining in France.

At 12:30 p.m. today I had a talk with Cariguel. He told me that the market had not been helped by the debate.

END OF MESSAGE.

WILSON.

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