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## Roosevelt Warns W. P. A. To Stretch 700 Million

He Tells Williams Fund Must  
'Last Until March 1'

From the Herald Tribune Bureau

WASHINGTON, Oct. 13.—President Roosevelt instructed the Works Progress Administration today to hold its expenditures within the \$700,000,000 left from the \$1,455,000,000 Congress appropriated last June to be available until March 1. The President's warning was made known by Aubrey Williams, Deputy W. P. A. administrator, after a brief White House conference on the relief situation.

"The President told me that the balance in hand will have to last until March 1," said Mr. Williams. Dismissing persistent reports that Congress at the very outset would be asked to approve a deficiency appropriation perhaps to cover the months of January and February. The emergency relief appropriation of the last session was designed to cover only the first eight months of the current fiscal year. Congress fully expecting to deal with relief appropriations as one of its early major problems.

At the White House conference today Mr. Williams presented a breakdown of the relief agency's expenditures since July 1, showing the following outlays by months: July, \$201,000,000; August, \$201,000,000; September, \$198,000,000.

"We have hopes of stretching the money out as desired by the President," Mr. Williams added, "employment is increasing everywhere and the outlook is brighter than at any time in a year. I look for a steady increase in employment all over the United States and in all lines."

He said W. P. A. rolls now total 3,120,000.


TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

DATE October 14, 1938

TO Secretary Morgenthau

FROM Mr. Haas 

Meeting in the office of the Director of the Budget, October 13, 1938, 3 p.m.

Subject: Exchange of Wheat for Strategic Materials

Present: Daniel W. Bell, Acting Director, Bureau of the Budget  
Frederick J. Bailey, Assistant to the Director and Chief, Division of Research and Investigation, Bureau of the Budget  
Charles L. Dasher, Assistant to the Director, Bureau of the Budget  
Jesse W. Tapp, President, Federal Surplus Commodities Corporation  
F. R. Wilcox, Vice President, Federal Surplus Commodities Corporation  
H. E. Collins, Assistant Director, Branch of Supply, Procurement Division  
George C. Haas

Mr. Bell asked Mr. Tapp to explain the proposition of exchanging wheat for strategic materials and indicate its relation to the budget.

Mr. Tapp indicated the desirability of having in this country reserve supplies of strategic materials for use in times of emergency. He said that Secretary Wallace had talked to the President with regard to this matter, and that the President had asked Secretary Wallace to get in touch with Admiral Peoples. Mr. Tapp said that a group, including himself and Admiral Peoples, had worked out a specific proposal. This proposal he stated to be roughly as follows:

The Surplus Commodities Corporation would sell wheat to certain countries having tin or other strategic materials, such wheat to be purchased through funds obtained from a loan by the Export-Import Bank. These materials would be stored by and under the direction of the Procurement Division in some old ordinance building located in one of the Carolinas. The

Secretary Morgenthau - 2 -

strategic materials would thus form the collateral backing of a loan at the Export-Import Bank. Mr. Tapp pointed out that at this stage his organization and the Department of Agriculture would be completely out of the picture -- the only parties then involved would be the Export-Import Bank, these materials forming collateral for an outstanding loan, and the Procurement Division which would be responsible for the storage of the materials. The plan envisaged the liquidation of the Export-Import Bank loan through purchase of the materials by the Navy Department from funds to be authorized by Congress in some future appropriation.

One of the purposes in seeing the Director of the Budget, Mr. Tapp explained, had been to secure his agreement to place an item in the Navy Department budget to cover the purchase of the strategic materials to be acquired under the plan.

Mr. Bell pointed out the weaknesses of a proposal which hinged on an appropriation which had not yet been approved by Congress. He indicated also that placing the item in the Navy Department budget does not indicate that Congress will approve it. Mr. Bell pointed out further that several bills had been before Congress, asking for an appropriation for the purchase of strategic materials, and the President had in each case indicated that these bills were in conflict with the Administration's program. He stated that just today one of the bills came back from the White House marked by the President, indicating that he did not favor it. Mr. Bell said he did not see that there was any fundamental difference between this proposition and the bills in Congress providing for the purchase of strategic materials, although he did appreciate that the present plan, in addition to securing the strategic materials, resulted in the disposition of surplus wheat.

The meeting was adjourned.

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Captain Collins told me after the meeting that Admiral Peoples had some days ago submitted to the Secretary's office a report covering this whole proposition.

The elements in the proposal which you may wish to consider are:



Secretary Morgenthau - 3 -

(1) That the proposal involves an increase of \$20 millions in governmental expenditures (the plan contemplates that Congress will appropriate \$20 millions for the Navy Department to take these materials out from under the Export-Import Bank loan);

(2) That the complete execution of the plan is based upon receiving an appropriation which Congress has not yet authorized. This procedure may be questionable.

The Department of Agriculture is completely free and in the clear after it has received its funds, but the Export-Import Bank is "holding the bag," in that it has the strategic materials as collateral for one of its loans, and the Treasury Department is not in the clear since the Procurement Division, as the plan is not set up, acts as the custodian and warehouse of the materials. I understand that the plan could be modified so as to have the Navy Department perform this function, but that the Navy Department is reluctant to do this because of the implication involved that they proceeded toward carrying out a program before the necessary Congressional appropriation of the funds had been made.

Friday  
October 14, 1938  
10:41 a.m.

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HMJr: Hello.

Operator: Mr. Helvering. Go ahead.

HMJr: Hello.

Guy  
Helvering: Hello.

HMJr: Hello, Guy.

H: Yes.

HMJr: How are you?

H: Fine.

HMJr: Guy, I have in my office Mr. Joel Spingarn who is interested in the Association of Improvement of Negroes, and they want to apply to the Bureau in order to get a status for this organization which will make it - what is it - ah - income tax free or whatever you call it?

H: Yeah. Exemption.

HMJr: Exemption.

H: Uh huh.

HMJr: And I would appreciate it if you could see them, go into it and advise them how they should present their case to you so that they can adopt their organization to our rules.

H: Yeah.

HMJr: Now when could you see them?

H: Well, are they there now?

HMJr: They're in my office now.

H: Well, I could see them at eleven o'clock or then I have an eleven-thirty appointment.

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HMJr: Well, eleven o'clock would be fine.

H: Yeah. I can see them then or later in the afternoon.

HMJr: No, that would be perfect.

H: All right.

HMJr: And if you give them ah - I mean give them every assistance so that they can - they're neither of them lawyers.

H: Yeah.

HMJr: So that ah - they want to adapt it so they can get it if possible, still for this current year.

H: Yes.

HMJr: See?

H: All right.

HMJr: I'd appreciate it.

H: Yes, indeed.

HMJr: Thank you.

GROUP MEETING

October 14, 1938.  
11:00 A. M.

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Present: Mr. Oliphant  
Mr. Gaston  
Mr. Haas  
Mr. Taylor  
Mr. Upham  
Mr. Gibbons  
Mr. White  
Mr. Lochhead  
Mr. Bell  
Mr. McReynolds  
Mrs. Klotz

(Mr. McAvoy sets up camera for pictures of the 9:30 Group Meeting.)

H.M.Jr: O. K., Mac?

McReynolds: You want to (talking very low) bring up that Hopson case status this morning?

H.M.Jr: Yes.

McReynolds: I think Mr. Oliphant had better; it's in his division.

Klotz: Can't hear a word you say.

H.M.Jr: I can't hear Mac either.

Oliphant: What's that?

H.M.Jr: The Hopson case.

Oliphant: I have here a five-page memorandum of it; it's pretty long. I'm having a summary of it made so you can have it with you, for you to take with you.

H.M.Jr: Well, that will be better. Fine.

Oliphant: You want to know the number working on it?

H.M.Jr: Yes.

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Oliphant: Ten lawyers part time, ten lawyers all the time; that is on his income tax; and about thirty agents, accountants, and auditors. At one time there was a top of fifty.

H.M.Jr: How much on his income tax?

Oliphant: I didn't have that broken down.

H.M.Jr: But they are all .....

Oliphant: For all years, yes. And some very interesting things recently came in that indicated criminal actions. I asked about how much time it would take to develop that - how much time would lapse which that was being developed, and they said a good deal of time, because when you had thirty or forty auditors on it .....

H.M.Jr: O. K. What else, Mac?

McReynolds: Nothing more, except on that San Francisco thing - the Shenley case.

H.M.Jr: What case?

McReynolds: The Shenley case.

H.M.Jr: Oh yes.

McReynolds: I didn't get to talk to Cy last night; I talked to him after I talked to you; I think he'd like to talk to you about it. He didn't think.....

Upham: It would be unfortunate, from the standpoint of their examiner's force on the coast.

H.M.Jr: Listen; listen, Cy, Mr. Farley, not to exceed once a year, makes a personal request. Now Farley's been magnificent about this.

(Mr. Upham shows H.M.Jr. paper.)

I don't want to see anything about it.

Upham: This is what I said we'll do.

H.M.Jr: (Looks at paper.) That's all right.

Now, I mean, there are times to be reasonable, and times to be hardboiled, and this is one of the times to be reasonable. See? Take my advice.

Upham: It's about the worst case we could be asked to take care of.

H.M.Jr: The man's honest, isn't he? He's honest?

Upham: Yes, I think so.

H.M.Jr: Just like the case of that young man Cliff Woodrum wanted me to keep - a man in Farm Credit. Well, he's responsible for my appropriation, so I said if he wanted to get a cot and stay there ..... So he bought a cot for him and told him as long as he layed down on the cot and didn't bother me, O. K.

Upham: That's what we'll have to do here. We can't let him in the bank.

H.M.Jr: Going through all this new change, and this fellow was restless, and Cliff Woodrum writes me a letter and said, "Let's keep him on instead of letting him out," and for five years he's had this cot, and this little room, you know; never had any trouble around there. Openly and outwardly he's on the payroll, and all he did was lay there, and we got wonderful recommendations.

Once a year - not to exceed that - Farley makes a reasonable request.

Upham: This makes an unfortunate request on the examining staff on the coast. We'll do it.

H.M.Jr: There are times to be very hardboiled, and times to be reasonable. For five years Cliff Woodrum's man has been laying on the cot there. When your organization has as good a reputation as Farm Credit, you come and see me.

Gibbons: Seven years.

H.M.Jr: If the fellow wasn't honest I wouldn't keep him a second.

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Upham: They thought that they were being good to him and letting him retire.

H.M.Jr: I mean, this is one of the exceptional cases where you use horsesense. That's my advice.

Upham: O. K.

H.M.Jr: Very, very rarely does Farley ever call me himself. Cliff Woodrum's man is laying on the cot, five years, across the Hill. You know about this?

Bell: No, I don't.

H.M.Jr: You remember it don't you?

Oliphant: Very well.

H.M.Jr: I didn't know whether you knew about it or not.

Bell: No, I didn't.

H.M.Jr: It's a famous case; it's known as the "Woodrum Cot Case."

Upham: I was a little hard on Mac.

H.M.Jr: What?

Upham: I was a little hard on Mac about this.

H.M.Jr: Why?

Upham: But it's all right.

H.M.Jr: Take it from grandpa, this comes under the heading of horse-sense.

Gibbons: I've just finished a memo on the subject, which will be in.

H.M.Jr: No, no. This is - this is - it's only when - I don't think Farley calls me to exceed once a year.

McReynolds: I haven't got anything else except these items I don't think you can very well dispose of here at staff.

H.M.Jr: (Aside to Mrs. Klotz.)

What's this fellow's name?

McReynolds: Shenley.

H.M.Jr: (To Mrs. Klotz:) Just phone Bray and tell Mr. Farley, until further notice, Mr. Shenley .....

Upham: Will be retained, pending further consideration.

H.M.Jr: And for him to go to bed and have a good time.

Upham: We'll give him a cot.

Gaston: Just like a Director of the Anglo-California Bank.

H.M.Jr: Make him a director?

Gaston: I say, just like a director - they have three or four of them in that.

H.M.Jr: All right. After five years, when I recommend something like that, you are safe in taking my recommendation.

Upham: I am sure of that.

Oliphant: I'd like to state for the record that Farley's never asked me for anything, except twice, in five years, and when we were trying to remove (name not understood) - get a competent person in his place - we wanted a woman - he stood back of us magnificently.

Gibbons: I have never had him make a request on me; he'll say, "This is what I am told; look into it and see if we can go along with it."

Upham: I have a suspicion if he knew the facts in this case he wouldn't go along.

Gibbons: Why don't you do this: hold him temporarily; my suggestion would be for Cy to go up and see him.

Upham: I have a letter on that.

H.M.Jr: Let Delano do that.

Mac?



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McReynolds: Well, nothing. You might want to sign these. There is the one to Cliff Woodrum about the ....

H.M.Jr: .. cot case?

McReynolds: (Laughs) .... (Speaking too low.) ..... If you don't get around to it, it won't hurt anything.

H.M.Jr: Mr. Bell?

Bell: You recall I took up some time ago, the duty and the question of answering Straus' letter, and giving him permission to sell all their bonds locally - sell local bonds. I thought for a while that I wouldn't answer the letter, but do it all informally, but Eddie Foley's convinced me maybe it is better to have it in the file and not let them withdraw it, and that last paragraph (in letter) doesn't mean anything, but you might read it.

H.M.Jr: (Reads) Oh, you diplomat; when did you join the State Department?

Bell: Oh, I took a lesson from the General Counsel.

Oliphant: What's that dirty crack?

Gaston: He's got a lawyer advising him now.

H.M.Jr: I asked him when he joined the State Department, and he said he took lessons from the General Counsel's office.

(Telephone conversation with Mr. Tom Corcoran, at 11:14 A. M. attached.)

Friday  
October 14, 1938  
11:14 a.m.

HMJr: Hello.

Tom  
Corcoran: Yes, Mr. Secretary.

HMJr: How are you?

C: Fine, sir. And you?

HMJr: Very well. You remember you asked me about a certain man who is very prominent recently in the Electric Utility field?

C: Yes.

HMJr: Well, I find that we've had about fifty men working on the company, plus his own case. About -

C: Yes.

HMJr: About thirty lawyers and about twenty accountants. So that's well in hand.

C: Oh, good.

HMJr: You know what I'm talking about?

C: I know what you're talking about, sir.

HMJr: Now, the other thing. I wondered if the next time when you came to town whether you wouldn't talk with Oliphant and McReynolds about this movement which is on to put this - ah - the most powerful union of unions - the lawyers -

(Loud buzzing noise)

HMJr: Hello. Hello. Hello.

Operator: Yes. I'm trying to get him back. Just a minute.

HMJr: Hello.

C: Yes, Mr. Secretary.

HMJr: There's a movement on to put the union of unions, the Lawyers' Union, the most powerful union in the world, under Civil Service. See?

C: Yes.

HMJr: And - I don't know whether you know anything about it or not, but next time you're in town have a talk with Oliphant and McReynolds about it.

C: I will, sir.

HMJr: And see whether you want to get in on it.

C: All right, sir.

HMJr: As far as I'm concerned I'm ag'in the Lawyers' Union, see?

C: So am I.

HMJr: You are too?

C: Yes.

HMJr: But, I think you'd be interested. There's quite a movement on; I don't know which is right. But McReynolds and Oliphant would love to talk to you about it.

C: All right, sir.

HMJr: Right.

C: Thank you very much, sir.

HMJr: Goodbye.

C: Goodbye.

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H.M.Jr: He says he's against the lawyers also.

McReynolds: Who's that, Eddie?

H.M.Jr: No, that's Tom Corcoran.

Gibbons: Did you know Eddy's office is divided on Dewey and Lehman?

H.M.Jr: (Holds side conversation with Mrs. Klotz.)

Bell: Last year we agreed to buy up to a hundred fifty million dollars, at par - that amount of Home Owner's Loan obligations, and then at the end of each month they would retire them out of their sinking fund. That agreement ends the fifteenth and they'd like to go on with that another year.

H.M.Jr: (To Mr. McAvoy, the photographer.) What do you want me to do, make a speech or something?

McAvoy: No, no, that's all right.

H.M.Jr: Want to do one more?

McAvoy: I'd like to get some pictures of you, personally, afterward.

H.M.Jr: You got all you want here?

McAvoy: Yes, we're all right on the group.

H.M.Jr: How about leaving your machine ....

McAvoy: Surely, I'll just leave it then.

H.M.Jr: .... and wait outside.

Bell: I think we ought to do that another year, Mr. Secretary, on the same basis we did before.

H.M.Jr: Start over again.

Bell: Well, we agreed last year to buy up to a hundred fifty million dollars of the obligations of the Home Owner's Loan obligations, and every month they would retire what we purchased the previous month, out of their sinking fund. I think we ought to do that another year, and when we get legislation .....

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H.M.Jr: All right with you, Wayne?

Taylor: I agree with Dan; it's a stop-gap arrangement, and isn't a good arrangement, but under the circumstances, it's the best thing we could do.

Bell: That's right. As you recall we would not permit them to go to Congress last year and get legislation on it.

H.M.Jr: Vaguely; I don't say I recall something I don't distinctly remember. I reserve the right to say I don't.

Bell: You asked me the other day to fix up a new rate for Jesse Jones at one per cent, and I was under the impression, at the time that we would - hadn't done anything for him since July 1, and I understand we did reduce the rate from two per cent to one and one half per cent on July 16.

H.M.Jr: That was previous.

Bell: That was on July 1. You still want to go down to one per cent?

H.M.Jr: Give him the works.

Bell: Last year we appointed a committee to look into the payroll procedure of the Department and there was quite a lengthy report made, and quite a complicated one; you have never had time to go over that, but what's worrying me now, we've had a letter on our desk from the Secretary of Agriculture, which hasn't been answered. I wonder if you would mind, and Mr. McReynolds would mind, turning this report over to Mr. Jump, in the Department of Agriculture and getting his reaction to it?

H.M.Jr: He's a good man.

McReynolds: Fine.

H.M.Jr: (Nods to Mr. Lochhead.)

Lochhead: We have the check ready for the advance payment on that last shipment of silver; it hasn't come in yet, but it is expected .... (words indistinct).

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H.M.Jr: I don't expect to get back until Wednesday night; why hold it up?

Lochhead: Fine.

H.M.Jr: Open the usual bottle of Sherry.

Lochhead: You will be interested to know how the Japanese discovered how to finance the war. (Hands H.M.Jr. broad tape clipping.)

H.M.Jr: "Shanghai. Japanese forces reported today that a Chinese artillery shell which struck a hillside in the Yangsin sector of the Hankow front uncovered a rich vein of gold ore."

Haas: Silver lining - no gold lining.

Lochhead: The sterling rate which went up as high as  $4.74\frac{1}{2}$  is down to  $4.73\frac{7}{8}$ . The London Press is going to ask .... (words indistinct - speaking too rapidly.) ... furnishing the market.

H.M.Jr: Did you see that story?

Gaston: I did. I did.

H.M.Jr: Who is the high Treasury official?

Gaston: I have no idea who the high Treasury official is.

H.M.Jr: If we follow it, then it will come back - it will be, "Aren't you going to answer it?"

Gaston: Crider talked to me before he came in to the conference; remember, he asked a question in the conference ..... (Mr. Gaston and two others talking at the same time.)

Taylor: He talked to me after your press conference.

Oliphant: Oh, you're the high Treasury official.

H.M.Jr: So you're the fellow; you're the fellow. Did he talk to you - the Times fellow? Is that what you told him?

Taylor: Part of it.

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H.M.Jr: I see.

Gaston: I think the story is not going to do any harm.

Oliphant: No, it's good preparation.

H.M.Jr: It's all right. I just wondered whether - if Archie had been talking again.

Taylor: Good.

H.M.Jr: Well, this is - confession is always good for the soul.

McReynolds: You never can tell what Archie will do on vacation.

H.M.Jr: I thought this thing through, and thought if we said anything about it, and he said, "Aren't you for it, I'd have to say, 'Yes.'" You read it all the way through, and there is just one little sentence of what I said.

Taylor: That was the one where he was quoting you. See, I said, you can price that and get around these various things, and so on. You think you'd do it about like this. Completely unofficial, see?

H.M.Jr: All right; so I gathered. O. K.

Lochhead: I might mention the Brazilian credit the State Department's extending them; they are working on that full speed now. We hope to get it set up today.

H.M.Jr: Wayne, will you take up with whoever the proper authorities are in the State Department, and tell them that I, as Secretary of the Treasury, wish the Brazilian Embassy would bring up a Financial Attache so I could do business with them. I think it is important enough and I lay considerable stress on it.

Taylor: Yes sir.

H.M.Jr: And the sooner the better; that I want the Brazilian Embassy to have a first-class Financial Attache who knows his business. The sooner the better.

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Taylor: I think it's a swell idea.

H.M.Jr: I am laying considerable stress on it.

Taylor: We have .....

H.M.Jr: Oh, it's just terrible.

Taylor: Well, we have been getting - I got a letter, in longhand from Warren Pierson, for example, yesterday, written down there, and the one thing that he was talking about was how important Brazil was and how things that bogged down - what he'd been talking about - had been misunderstood by our Embassy down there, and in turn gotten mixed up here.

H.M.Jr: I think it's easier to have a Financial Attache here than to have them put a new American Ambassador down there.

Taylor: Much easier.

H.M.Jr: Tell them I lay considerable stress on it.

And Herbert, sometime I wish you'd put your mind on this thing, and I want to work out some publicity in connection with this Brazilian deal. They are sending up a million dollars under that original sixty million, you see, and establishing a credit here.

Gaston: Yes, yes.

H.M.Jr: I'd like to work out with Brazil - something to give them some publicity.

Gaston: In connection with the million dollars worth of gold they are going to take.

Lochhead: They are borrowing against a million which they are sending up. One thing more; I mentioned yesterday that the British had sent over gold which they have earmarked to a total of about ninety million dollars, and yesterday they sold out fifty million of that, and we got a cable this morning to sell out the remainder to meet sales, and so they've sold out all of their gold.



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H.M.Jr: All of it?

Lochhead: All that is here. They are sending more.

H.M.Jr: Fine. (Nods to Mr. White.)

White: Here are the comments you asked for, preceded by a summary which I think is very interesting, and the digest on foreign exchange rates. I thought it might be significant in that last column to see the changes that occurred on the dollar all over the world.

H.M.Jr: Bring this up with you to the farm, will you? Bring that up, will you?

White: Then I will talk about it then. That's all. Wayne, there is something about Peru.

Taylor: Yes, I want to talk about Peru.

H.M.Jr: I didn't read any of the things you gave me last night; I'll take them to the country with me.

Taylor: On the Peruvian thing, Harry and I figured there is some possibility in the Peruvian situation which should be explored with the idea of using them as kind of a guinea-pig.

H.M.Jr: O. K.

Taylor: It can't hurt us any, and might do us some good.

H.M.Jr: Who's idea was this?

White: Joint.

Taylor: It's a joint idea.

H.M.Jf: If, when Harry's up to the farm Monday - if you have any time, Harry, talk "guinea-pig" to me.

White: (Nods "Yes.")

H.M.Jr: Anything else, Harry?

White: That's all.

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H.M.Jr: Incidentally, I think if you get there by eleven is time enough.

White: Plenty.

H.M.Jr: I am going to have my horseback ride first.

White: I heard you say you wouldn't be back until Wednesday night?

H.M.Jr: I did. I want to see the President on Tuesday.

White: I want to spend the day in New York.

H.M.Jr: All right. Just get Mrs. Klotz' O. K. on it.

White: I will, if I can.

H.M.Jr: (Nods to Mr. Gibbons.)

Gibbons: I'm giving you a memorandum to take with you on some political stuff - two telephone calls I have had; one from Drew Pearson and one from Mr. Ickes, about changing Collectors - Comptrollers of Customs, not in line with the New Deal.

H.M.Jr: In Maryland?

Gibbons: In Maryland and Georgia.

H.M.Jr: "Maryland, My Maryland." We've got some new ones - Mr. Ickes and Mr. Drew Pearson.

Gibbons: Well, they are working hand in hand. I suggested that Mr. Pearson talk to Mr. Farley.

Klotz: Taylor's having a good time.

H.M.Jr: What?

Klotz: Taylor's having a good time.

Taylor: It's a free state.

H.M.Jr: (Nods to Mr. Upham.)

Upham: I just learned this before I came in and I haven't had time to think about it very long, and I may be going off half cocked.

H.M.Jr: That's possible. (Laughter)

Upham: Ben Smith, who was recently in Europe .....

H.M.Jr: Yeah.

Upham: .... and before he went, he got a list of stocks, large blocks of which are owned by the Insolvent Bank Division of the Comptroller's Office, and made some deals over there whereby he could sell them for us; and he's now back and wants to know with whom he should discuss the matter. Well, it just struck me, offhand, a little unusual that we would supply lists of holdings to private individuals to dicker with, but after all, I suppose what we want to do is get rid of them, and it may be all right, but I wanted to talk to some of the people about it, and wanted you to know about it before you left.

H.M.Jr: Well, as Peter Stuyvesant says in the play, "It doesn't smell right."

Upham: At first small, I thought not.

McReynolds: Cy hasn't got educated to that - that continual .....

Oliphant: Of all men.

Taylor: No, there is - I don't - if you've got a list of securities that are for sale, for liquidation, well, you've got to go to somebody who's in the securities business, and it's a free country.

Oliphant: How well Smith knows it's free country.

Taylor: Yeah.

Upham: His Washington intermediary was Amil Hoguet.  
(Laughter)

Gaston: Well, that's liederkranz; at first it smelled like limburger, but now it's liederkranz. Mr. Taylor .....

Taylor: Mr. Taylor talked to him this morning and took him around to see Mr. Upham.

Gibbons: I told him Mr. Taylor wouldn't talk to anybody about Customs, and the thing for him to do was go around and see Mr. Taylor.

H.M.Jr: Anything else?

Upham: That's all.

H.M.Jr: Well, I invited a gentleman to succeed you - notice I didn't say to take your place - and he is coming in the first of November. Mr. Duffield.

Upham: Splendid.

H.M.Jr: I arranged it last night; I called up his publisher and he said he'd give him a leave of absence.

Upham: Wonderful.

Taylor: Very good.

H.M.Jr: Well, how do you like it?

Gaston: I don't know who it is.

H.M.Jr: Duffield - Gene Duffield.

Gaston: Oh!

H.M.Jr: To take Upham's place.

Gaston: Fine, fine; very fine, indeed.

Upham: I'll have to make good where I am now.

H.M.Jr: I invited him - I called up Hogate last night and told him I wanted him, and he said he wouldn't give him a guarantee they would take him back, but if things were then as the are, they would take him back. Duffield, I don't think - I don't know when he wants to announce it. He isn't coming till the first of November. I think the first thing we'll do is start him on a trip around the country.

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Upham: He has succeeded me before.

H.M.Jr: Has he; where?

Upham: He worked for me at the United States Daily.

H.M.Jr: Well, I think .....

McReynolds: He's following you up, Cy.

H.M.Jr: He's as good a man as I know of to do the things you used to do for me. As I say, we'll start him out on a trip around the country - Smith - on this bank business.

Gaston: Yes, very good.

Upham: That's all.

H.M.Jr: (Nods to Mr. Taylor.)

Taylor: While you were abroad, you sent .....

H.M.Jr: You might send for Duffield and have a talk with him, will you; ask him whether he'd like to - ask him when he wants it announced, will you do that?

Gaston: I'll do that today.

McReynolds: And have him come in and see me.

H.M.Jr: I told him to come in and see Mac this afternoon, and talk salary with him; when he comes in this afternoon then he can go down and see Herbert.

Taylor: While you were abroad, see ....

H.M.Jr: Yeah.

Taylor: ..... you sent a cable from Paris, about two people who were working in the Embassy, in the Code Room, and so on, recommending that if it were legally possible you'd like to have them paid especially out of the Stabilization Funds. We talked about it here, and also talked about it a little bit over in the State Department, and we didn't think it was a terribly desirable thing to do, for various reasons.

There is another request, a similar request, that has come in now from London about somebody else who is working there, and so on.

H.M.Jr: I thought it had been done; hasn't it been done?

McReynolds: No.

Taylor: No, and yesterday when I was going through some things to talk to you about, why, I got these two cables; this cable you sent, and I thought Mac and I had better talk to you about it again.

McReynolds: Yes, because Bolton is in town; he's coming in in a little while.

H.M.Jr: You'd better give me a - bring something in on it.

McReynolds: They are on the regular roll.

Oliphant: -- supplemental payment out of it.

Taylor: These are straight State Department employees.

(Mr. McReynolds and Mr. Taylor talking together.)

Lochhead: What about your announcement, of Butterworth and Cochran?

H.M.Jr: Well, please have it when I come back Wednesday - have it for me, will you?

Wayne, I sent in your office, some telegram that McAdoo wanted something. Just acknowledge it and clean it up one way or the other for me.

Taylor: What we were waiting for was Mr. Fox to call somebody up; we have never heard a word from Mr. Fox.

H.M.Jr: Will you communicate with McAdoo?

Klotz: We haven't acknowledged it, and we have always acknowledged them.

Taylor: What it is about is the San Diego Border, etc.

Klotz: We were just waiting until this man came in. Two people wrote about it, McAdoo and somebody else.

Taylor: A fellow by the name of Izac.

Klotz: I didn't acknowledge it because the Secretary wanted you to see it, see?

H.M.Jr: Just see that the two communications of these people get some kind of an acknowledgement today, so that McAdoo - simply say, "We've got your telegram, and when the people come in we'll see them," that's all. O. K.?

Taylor: Oke. But I am still confused about it.

H.M.Jr: Why?

Taylor: There's the two wires about some guy by the name of Fox who is going to be in town here and who is going to call ....

H.M.Jr: ... for an appointment.

Taylor: And he says, "Please see him." Sure, we'll see him.

H.M.Jr: That's all you've got to say. When I get telegrams and refer them to somebody to see them, that means that we haven't acknowledged them, and I don't like to leave them go unacknowledged. Simply say, "Your telegram received and Mr. Morgenthau asked me to see these two fellows when they come in, but to date we haven't seen them."

Gibbons: Are you talking about this Fox, from California? I talked to him yesterday. Kieley sent him down to see me. He wanted to see you.

H.M.Jr: Will you send the telegrams to Steve; I want McAdoo and Izac to get an acknowledgment. Taylor will send them to you, and we'll have them acknowledged today. That's all we want.

Taylor: It was Steve's business and I knew it was. He never came in.

Klotz: (Speaks to Mr. Taylor at same time H.M.Jr. talking to Mr. Oliphant.)

H.M.Jr: All right, Wayne?

Taylor: Sure.

H.M.Jr: All right. George?

Haas: I attended that meeting that Dan asked me to go over, when Tapp came over, on the proposal to exchange wheat for these strategic war materials. I'll send you a memorandum to keep you up on that.

H.M.Jr: (Over telephone:) Frederic Delano, wherever he is.

George, one thing I want, and my time is very short. You had a lot of charts prepared in connection with labor, employment, and going into it on a kind of temporary basis, added so-and-so and took off some.

Haas: On that transparent material.

H.M.Jr: Where is that now?

Haas: In my office.

H.M.Jr: Give it to Harry when he comes up Monday. I want to use it for the President.

Haas: You don't want me to talk about this other thing?

H.M.Jr: I haven't got time. I talked to Bell. We have to have a meeting in the Treasury. Bell and I both are all confused. Shall we tell them why?

Bell: I am going to take it to the White House with me today and see what his policy is on this thing. The thing you've got to decide is whether you want the Procurement Division to hold the bag. And if War-Navy steps out from under it ..... They are perfectly willing - they are, in effect, creating deficiencies in the appropriation, and have to depend on Congress to appropriate money. In the meanwhile the Procurement Division is holding the bag.

H.M.Jr: Back of that, tell them what the President turned down.

Bell: The President yesterday turned down legislation proposing that very thing - purchasing of strategic war materials.



H.M.Jr: That is being contrary to his policy.

White: I thought, moreover, it wasn't practical, unless something new developed.

H.M.Jr: Well, get George to tell you. Yesterday, or within the last forty-eight hours, the President turns down .....

(Telephone record of conversation between H.M.Jr. and Mr. Frederic A. Delano, at 11:40 A. M., attached.)

Friday  
October 14, 1938  
11:40 a.m.

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Frederic A.  
Delano: --- Fine, thank you.

HMJr: Are you in this city?

D: I am. (Laughs)

HMJr: Ah, Mr. Delano, I had a chance to talk with the President about this idea of -

D: Yes.

HMJr: - getting together with - have an informal fiscal committee -

D: Yes.

HMJr: I don't know whether you've seen him or not on it.

D: No, I have not.

HMJr: Well, as I put it to him, we'd try it on a trial-marriage basis.

C: Yes.

HMJr: He said no, he wouldn't call it that but he said he'd give you a free pass for this season -

D: (Laughs)

HMJr: - to the ball games.

D: Well -

HMJr: So, ah -

D: That's all right.

HMJr: Ah - what I thought was this - that next Thursday I'd be glad to have the first meeting at two-fifteen at my office if that would -

D: Yes.

HMJr: - be convenient to you.

D: All right.

HMJr: Now -

D: Wait until I look at my calendar.

HMJr: Will you please. - Next Thursday at two-fifteen.

D: Yes. Of course, I think this, that ah - ah - I like informality and yet if there isn't a certain amount of formality the thing is ah - is not taken seriously.

HMJr: Well, I - I'm - I'm in dead earnest about it; I'm going to - if I don't get -

D: Well, that would be Thursday the twentieth?

HMJr: Yes.

D: All right, sir.

HMJr: Now who will come?

D: Well, ah - if you don't object I think that I'd better bring Rumel. If I come with Rumel is that agreeable to you?

HMJr: Ah - any - any - that's all right.

D: The reason I suggest that is that ah - I wouldn't like to come alone and then retell to my colleagues -

HMJr: That's all right.

D: - what was done. And ah - there is disposition on the part of our committee to - to have two if you didn't object to it.

HMJr: No, that's quite all right.

D: All right.

HMJr: Two-fifteen next Thursday.

D: Two-thirty?

HMJr: Yes.- Two-fifteen.

D: Two-fifteen? Thank you very much.

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HMJr: A quarter past two.

D: Yeah. Thank you.

HMJr: Thank you.

H.M.Jr: Is that all right with you, Dan?

Bell: (Nods "Yes.")

H.M.Jr: And I want Dan there, and Taylor, Hanes, Cox, and Eccles. And then if you could, in preparation for that, eleven o'clock Thursday, to have ..... (speaking low) Let's have either Hopkins or Aubrey Williams come over and give us the latest figures on how they are going to plan this unemployment. We'll have that for the afternoon.

Bell: Is there anything else we might discuss at that time?

H.M.Jr: You be thinking about it, will you? He's bringing - it will be Delano and Ruml.

Klotz: In the afternoon?

H.M.Jr: What?

Klotz: In the afternoon?

H.M.Jr: Two fifteen. Eleven o'clock for Hopkins, and two fifteen for the so-called informal visit. Delano may not come; you'd better let our own people know. In the morning Bell will try to get Hopkins and Williams and ..... (low) We'll have that for the afternoon meeting.

Bell: All right.

Haas: The only other thing is a very minor thing. Tapp is very busy over there trying to learn the signals on this. If he wasn't able to see me until Monday, would it bother you? I mean, you won't be back anyway; they're all jumbled up over there - don't know who's got the ball.

Bell: They ought to be used to that.

H.M.Jr: Sure, that's all right.

I'll tell you an awfully good joke on myself. At yesterday's press conference when I said this was the best thing Wallace ever did, I thought he was giving this away; I didn't know he was selling it

at a low price. It was a joke on me. I thought he was going to take care of these unemployed and give them the food, the way we did in May and June. I didn't know he was going to sell it.

White: This has greater possibilities.

H.M.Jr: I am not going to correct it; I'll let it ride. I am not going to correct it.

Gaston: Monday, the Tribune had some extravagant mis-statements in its lead about the Social Security funds - the usual sort of thing. I wrote to Jerry Parsons, of the Herald-Tribune, a rather mournful letter on the subject, which Morris Collins looked over and approved. Parsons wrote me today and asked if he could print the letter, so if it's all right with you, I can tell him he can print the letter.

Bell: It's a good letter.

H.M.Jr: Fine.

Gaston: I have here - you saw the order on net prices little gain? There is a press release; I think you will find it's all right.

H.M.Jr: All right.

Gaston: There is something Dr. Parran wants to run, as a forward to the program. It's O. K.

H.M.Jr: I never saw it. If it's terrible, I'll have to say I never saw it.

Gaston: I'll have to forge your signature.

H.M.Jr: It's all right? You say it's all right?

Gaston: It's all right.

H.M.Jr: O. K.

Bell: By the way, Aubrey Williams is being put on the Interdepartmental Health Committee.

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Oliphant: One of the first questions that Chen asked Morris Collins when he began to talk with him was who would he suggest as Director, and Morris talked about it afterward to me.

H.M.Jr: Weren't you here when I gave him the list of names?

Oliphant: Yes - just reporting to you; I didn't see any objection to that.

H.M.Jr: For putting his father on it?

Oliphant: No, to talk it over with his father. I should think it would be desirable for Morris is handling it for him, for he has that list of names.

H.M.Jr: On Thursday. Have you got that list?

White: Yes.

Lochhead: I have - Miss Chauncey gave me the list; I've got the names of the men.

H.M.Jr: Anything else.

Oliphant: We'll have to have your signature to an affidavit we are going to use in the promotion for the Spanish suffrage cases. Shall we sent it up to you to be signed Monday?

H.M.Jr: Harry can bring it up and bring it back. It will be Monday; he won't be there Tuesday.

Oliphant: If it didn't happen to be ready, would it be all right to mail it? There will be mail going up Tuesday, won't there?

H.M.Jr: I wouldn't rely on the mail.

October 14, 1938  
11:45 a.m.

ADDRESSING LIEUTENANT R. L. BURKE, USCG

On June 13, 1933, a Coast Guard plane piloted by you flew from Gloucester, Massachusetts, to a position about 130 miles off the Massachusetts coast where you took aboard the plane from the fishing trawler SHAWMUT a critically injured seaman and transported him to Boston where he was taken to a hospital by an ambulance. His life was saved. In making this flight you flew through rain and fog, depending upon radio bearings to guide you on your course and locating the position of the SHAWMUT through the use of the plane's direction finder. A heavy ocean swell added to the difficulty of landing and taking off from alongside the SHAWMUT.

In making this flight you demonstrated resourcefulness, courage, ability and skill of an outstanding



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character, and in recognition of your heroic action and extraordinary achievement, it is my pleasure and privilege to present to you, on behalf of the President of the United States, the Distinguished Flying Cross, pursuant to Act of Congress of July 2, 1926, as amended.

I may say that while you have been awarded this coveted decoration primarily for your service in an aerial flight to rescue a seaman from the SHAWMUT, the official records show that you have participated in five other outstanding aerial flights involving the saving of life of injured or seriously ill persons. Your services in such respect are in keeping with the highest traditions of the Coast Guard and have reflected great credit upon you individually and upon the Service of which you are a member. My congratulations and admiration.

October 14, 1938.

MEMORANDUM

TO: Surgeon General Parran  
FROM: Mr. Gaston

With reference to your letter of October 11th to the Secretary and the accompanying foreword for the program of the dedication ceremonies of the Fort Worth hospital, the Secretary has authorized me to give you his approval.

Attachment.



IN REPLYING  
ADDRESS THE SURGEON GENERAL  
U. S. PUBLIC HEALTH SERVICE

TREASURY DEPARTMENT  
U. S. PUBLIC HEALTH SERVICE  
WASHINGTON

October 11, 1938

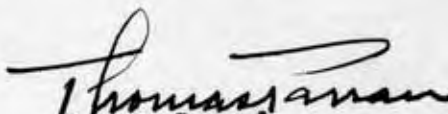
The Honorable

The Secretary of the Treasury

My dear Mr. Secretary:

There is enclosed herewith, for your consideration and approval, a short statement that it is desired to place on the program for the dedication ceremonies of the United States Public Health Service Hospital, Fort Worth, Texas.

Very sincerely yours,

  
Surgeon General

Enclosure

FOREWORD

The first hospital established by the Government for the treatment of drug addicts was opened at Lexington, Kentucky, in 1935. The dedication of the United States Public Health Service Hospital, Fort Worth, Texas, is therefore the second milestone in progress towards the scientific handling and treatment of persons suffering with narcotic drug addiction.

Under the policy inaugurated with the inception of these two hospitals there is put into practical operation a humane and scientific plan for the handling and treatment of addicts and for the study of drug addiction, to the end that more knowledge may be obtained and applied to the treatment and rehabilitation of a group of patients whose fundamental difficulties and needs have been neglected because they have been only vaguely understood.

The work of rehabilitation will include industrial, educational, and vocational activities in addition to the strictly medical treatment, and the information gained through research will be made available for general application to the solution of a problem which is of vital concern to the entire country.

Secretary of the Treasury

RECEIVED  
 DIVISION OF INVESTIGATION  
 MAR 8 1938  
 SECRETARY OF THE TREASURY  
 OFFICE

My dear Mr. Secretary:

I want you to know that the employees of the Tabulating Section of Accounts & Deposits, in the Printcraft Building, (about whose "sweat-shop" working conditions I wrote you on September 26th) - are deeply grateful for the prompt and fair manner in which you adjusted their difficulties. Several new employees were taken on and the excessive overtime was almost immediately discontinued, and when it is necessary now to do any overtime it is compensated for with time off during the week.

I did not tell anyone at the time that I was writing to you because I did not know if my letter would reach you; but I did know that if this matter could be brought to your personal attention you would remedy the injustice, and that is why -- when everything else failed -- I took the liberty of writing to you.

When the change came everyone was so surprised and wondered, and I then told a few of them what I did, and that you were responsible for the improved conditions. They do thank you, and everyone is happy now and life is worth living again. You can certainly have a feeling of satisfaction for having done this fine thing.

Thank you, again!

(I'd like to sign my name, but  
I just wouldn't dare!)

Honorable Henry Morgenthau, Jr.,  
Secretary of the Treasury,  
Washington, D C.

October 14, 1938.

EG

PLAIN

London

Dated October 14, 1938

Rec'd 9:22 a.m.

Secretary of State,  
Washington.

1183, October 14, 1 p.m.

FOR TREASURY FROM BUTTERWORTH.

The dollar opened slightly bid at 4.73 and after moving to  $4.72\frac{1}{2}$  reacted on natural offerings to  $4.73\frac{1}{4}$ . The British authorities gave dollars at about this level until gold fixing. They supplied the overwhelming majority of the 468 bars at 146S.10D. And although the price was called parity, in reality it was at about  $1/2D$  discount. With the offering of dollars incident to gold fixing the rate moved to  $4.74\frac{1}{2}$ , later  $1/4$  at which point official offerings were forthcoming. The volume of trading has only been fairly large and there was some tendency to take profits prior to the weekend. Two other factors tended to reduce the amount of pound selling: (1) The Chancellor of the Exchequer's reference in a speech of last night to "The urgent need for economy in all permissible directions" and (2) An ambiguous Reuter report quoting an article in the NEW YORK TIMES regarding the intention

-2- #1183, October 14, 1 p.m. from London

intention of the Administration to obtain from the next Congress agreement "to extend the President's power to devalue the dollar". Apparently in some continental quarters the word "extend" was taken to mean an extension in amount, not in time.

The comment in today's financial press takes the line that the position is not as bad as "the foreigner" assumes it to be. In connection with my 1178, October 13, 7 p.m., the following excerpt from the city column of today's TIMES may be of interest. "There were not many people a week ago even among the definite pessimists who would have forecast quite such unsatisfactory markets as we have seen so far since the beginning of the new account. The substantial falls in prices and the paucity of business which have characterized these last four days hardly reflect the views which most London operators held last weekend. But in a security market which remains in a considerable degree international we must perforce see ourselves as others see us; and it is necessary to bow to some extent to the foreign view of our financial prospects even if perhaps in disagreement with it. London might indeed be permitted to feel a little academic resentment at the fact that Continentals and others take so severe a view of

of

-3- #1183, October 14, 1 p.m. from London

of our financial and political prospects when we may at least claim that our armed security is not less and our budgetary soundness even on the worst assumptions considerably greater than their own. That there should be a natural propensity to seek a refuge for funds in America is understandable. But during the past day or two it has been difficult to ignore the fact that the movement has in part assumed more directly the character of a flight from sterling and the London market as such. The leading continental currencies have indeed been becoming rather more immune from the effects of the flight. This outbreak of foreign distrust, which has naturally affected an already hesitant domestic sentiment, may reasonably be regarded as exaggerated to the point of being a definite miscalculation. It is difficult to feel in fact that the prospect is as bleak as the heavy allround break in markets during the past four days would imply. But meanwhile we cannot be blind to the fact that London is in thorough disfavor with oversea operators and the comparison between London and New York is undeniably odious. The flight into the dollar and United States securities and the flight out of sterling and sterling securities are now almost two distinct components of the current movement.

KENNEDY



AM

OFFICE CORRESPONDENCE

DATE October 14, 1958.CONFIDENTIAL FILESSUBJECT: TELEPHONE CONVERSATION WITHL. W. KnokeBANK OF ENGLAND.

Mr. Bolton called me at 12:05. He had supported the market all afternoon and had been selling dollars on the Continent partly through foreign central banks, partly through the London branches of American banks. As a result there had been a slightly better tendency for sterling but nevertheless he had had to sell so far \$12,000,000 ( of which \$8,000,000 through the National Bank of Switzerland which had acted for him in Zurich). He had had to have resort to that sort of thing today to "prevent a run-away rate and give the market a somewhat better tendency." There had been a great deal of speculation in Paris on the part of Lazard and Dreyfuss and efforts to manipulate the market. They had just received a report at the bank that the Agence Economique had planned in a broadcast tonight over a private radio station to make the statement that sterling was going to be devalued over the weekend by at least 10 per cent. This report had reached them in time to make certain of a denial of any such rumor in the press tonight. Since we might hear of or read these rumors he wanted me to know the background and what they had done about it. Needless to say there was positively no intention on the part of the Government to devalue. This report in his opinion was part of a deliberate propoganda based on the fact that people believed that sterling was bound to fall.

Mr. Bolton then gave me a new lower selling price for

FEDERAL RESERVE BANK  
OF NEW YORK

45

OFFICE CORRESPONDENCE

DATE October 14, 1933.

CONFIDENTIAL FILES

SUBJECT TELEPHONE CONVERSATION WITH

L. W. Knoke

BANK OF ENGLAND.

2

gold (146s 9d) "so that you can go into the market tonight." Was it his plan that we should operate, I asked, and Bolton replied "if you would be good enough to do that."

One of the things that had helped sterling today, Bolton continued, was the report that the President intended to extend his devaluation powers. This kind of prompt reaction to rumors of that sort was very characteristic of the psychology of the market. It would take some time for the British to get through this and then it would be quite expensive for them; expensive, that is, to hold the rate where it is now. If the pressure continued they would probably have to reconsider. I suggested that he probably wouldn't care to go through ten more days like yesterday and Bolton replied that they could not afford to.

LWK:KW

EG

PLAIN

London

Dated October 14, 1938

Rec'd 3:20 p.m.

Secretary of State,  
Washington.

1187, October 14, 5 p.m.

FOR TREASURY FROM BUTTENWORTH.

The movements in the dollar-sterling rate since my 1183, October 14, 1 p.m. have been as follows. After holding the rate at 4.74 1/8 the British authorities went out of the market and the rate slipped back to 4.73 7/8 but Paris reopened in the afternoon the seller of dollars and the rate moved to 4.74 5/8 at which point New York came in a buyer of dollars and the rate moved back to 3 3/4. The British authorities have given support to the pound since then and are at present holding the rate at 4.73 5/8. The volume of trading has not been large this afternoon but the factors favorable to market sentiment mentioned in the first paragraph of this morning's telegram have been nullified by New York coming in as a seller. Furthermore, the general feeling in the city continues uneasy and British security markets were inclined to be weak. The franc has been steady and the amount of selling limited.

KENNEDY

WVC

## PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris

DATE: October 14, 6 p.m.

NO.: 1755

FROM COCHRAN

A newspaper report from Amsterdam states that Dutch bankers credit to France which expires October 20 has been extended for three months for an amount of 35,000,000 florins. For details of this credit, see my 1233 of August 8, 4 p.m. This credit should not be confused with the Mendelssohn loan authorized for 150,000,000 florins which matures in part around November 20 and regarding which I quoted President Trip in my 1730 of October 11, 9 a.m.

At six p.m. I had a talk with Rueff of the French Ministry of Finance.

Rueff said that the above extension was automatic. With regard to French financial decrees he was still not certain as to when they will appear. The general opinion is that they will be delayed until after the senatorial elections of October 23, in view of the many developments in internal French politics.

I called the Bank of France around six o'clock. The British stabilization fund had lost 15,000,000 dollars

and

-2-

and one and a quarter million pounds in gold during the day and the French stabilization fund had lost 372,000 pounds. The rate of sterling has been jumpy.

WILSON

EA:DJW

RECEIVED

OCT 19 1938

TREASURY DEPARTMENT  
OFFICE OF THE ASSISTANT  
SECRETARY IN CHARGE

FS

GRAY

London

Dated October 15, 1938

Rec'd 10:40 a.m.

Secretary of State,  
Washington.

1189, October 15, 1 p.m.

FOR TREASURY FROM BUTTERWORTH.

With Paris closed and the city virtually deserted for the week-end, the volume of trading in the foreign exchange market has been small. The dollar opened at  $4.73\frac{3}{4}$  offered and has fluctuated near that level with no apparent intervention by the British authorities except that they put in most of the 281 bars at gold fixing at  $146/8\frac{1}{2}$  penny. There has been some bidding for the franc which moved to 178 11/16 but it is not certain whether the Bank of England was operating on commercial or intervention orders.

The city in general is still a bear of sterling. It expects that the recent stand by the British authorities will if necessary be repeated but that the likelihood is that sterling will continue on its course of depreciation. In this connection the tentative tone of the following excerpt from the city column of today's TIMES is of interest:

"The

FS 2- No. 1189, October 15, 1 p.m. from London

"The foreign exchange market derived a certain amount of adventitious assistance from the report that President Roosevelt was seeking reenactment of his currency powers which was transformed into a rumor that he actually had it in mind to devalue the dollar; indeed the melodramatic recovery in the dollar rate around the middle of yesterday was more or less wholly due to some large operators acting on this rumor.

(END SECTION ONE)

HPD

KENNEDY

MY

PLAIN

London

Dated October 15, 1938

Rec'd 10:45 a.m.

Secretary of State

Washington

1189, October 15, 1 p.m. (Section two).

"None the less even apart from the special factors involved it was generally a much more satisfactory day both for the London security markets and for sterling. A very definite halt was called to the runaway trend which had been gathering momentum during the week. It is clear that an important stage has now been reached. It may be that yesterday's relative steadiness was no more than a temporary exhaustion of the forces which have been depressing sterling and the London security markets. But at the same time there is no doubt that the foreign apprehensions which have inspired those forces have been exaggerated and there is now at least a potential interval in which a calmer view may have time to emerge. The exchange account has certainly made a more definite effort to check the decline in sterling during the past two days and it is just possible that it may have found the psychological moment to make a more determined defence effective. The support given by the control



MY -2- No. 1189, October 15, 1 p.m. from London.

control on Thursday was considerable. Yesterday it was possible to keep sterling steady on balance without intervention on any large scale but the policy of selling substantial amounts of gold to arbitrageurs was continued and even expanded. It is conceivable that the major flight of funds from the London market may have been adequately interrupted. There are few people of course who do not expect a moderate flow of funds to New York to continue. But that is not quite on the same plane as the wholesale flight from all things sterling and the wholesale embrace of all things American which were witnessed during most of this week. A continued flow of funds to New York would still be consistent for example with a firmer security market in London and a diminished concentration on Wall Street which must have derived as much support for its rapid and substantial advance from London's abrupt unpopularity as from the real but still moderate improvement in American business conditions." . (End message)

KENNEDY

RR  
CSB

## PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Rio de Janeiro, Brazil

DATE: October 15, 1938, 1 p.m.

NO.: 244

Reference is made to my telegram No. 234 of  
October 8.

I have been told by the Director of Exchange that  
during the week of October 17 the Bank of Brazil will  
close exchange for maturities and daily quotas for the  
whole period September 1-27.

Will you please transmit to the Department of Commerce  
the above information.

CAFFERY.

EA:LWW

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE

54  
10-15-38

TO Secretary Morgenthau  
FROM Mr. White  
Subject: The Alleged Governmental Subsidy on Leather Goods  
Exported from Italy.

1. In a letter dated September 3, 1938, Mr. Arthur Wiesenberger reported that he had heard through domestic mercantile circles that the Italian Government is subsidizing the export of leather goods to the extent of 60 percent of their selling price. (A proposed acknowledgment of his letter is attached.)
2. The Bureau of Customs does not have any specific information concerning Italian governmental subsidies paid on leather goods exported to the United States. A search of consular reports and other material has not disclosed any information on this subject.
3. The Bureau of Customs does, however, have two reports from the United States Treasury Attache at Paris (dated February 27 and May 27, 1938) which indicate a probability that exports of cotton goods from Italy are being subsidized. According to the more recent of these reports, Italian exporters of cotton gloves are able to sell to the United States at about 50 percent below the foreign purchase price, being reimbursed for their loss by receiving permits to import cotton, which can be sold in Italy at a tremendous profit. In another connection it was reported to the Bureau of Customs that an American consul in Italy had obtained certain information with regard to a subsidy on the export of raw hides to the United States.
4. A request has just been sent to Paris for an immediate investigation of possible export subsidies in connection with the export of raw hides and leather goods. In view of the obstacles which are placed in the way of investigations by United States Treasury agents in Italy at the present time, no satisfactory and detailed report can be expected, at least without great delay.

Secretary Morgenthau - 2

5. It is suggested that the Treasury Agent at Milan be authorized to report in general terms concerning his understanding of the nature of Italian governmental subsidies to exporters, the extent to which subsidies are being used, the products subsidized, and the amount of the subsidies. The Bureau of Customs will not request such an investigation without specific authorization from you.

## TREASURY DEPARTMENT

## INTER OFFICE COMMUNICATION

DATE October 15, 1938

to Secretary Morgenthau

FROM Herman Oliphant

In re: Treasury aspects of Associated Gas and Electric System, and Howard C. Hopson's personal companies.

For your information, I have prepared a summary of the status of the pending cases involving the tax liabilities of the Associated Gas and Electric System and Howard C. Hopson's personal companies:

1. Board of Tax Appeals

There are forty-six cases now pending before the Board of Tax Appeals involving a total estimated tax liability of \$58,952,149.00 filed by the System companies. In addition there are thirty-five cases pending, involving \$6,568,493.00 filed by Hopson personally and by companies owned by him. The enormous task of preparing these cases for trial is illustrated by the following excerpt from a report of one of the revenue agents:

"Multitudes of transactions, passing through numerous records, going through five, six and seven companies' records to go from one company to another, bewildering reversals, switching from company to company continually, with no apparent reason to the uninitiated. Transactions travelling through a labyrinth that defies and discourages tracing, and even after building up a reasonable structure by tracing of securities to establish tax values of a 'First-in and First-out' method, probably through three or four companies for one security sale or a number of sales, we can only expect that the taxpayer will come along and identify one block passing from company to company which will slash through and destroy all 'First-in and First-out' computations of accounts through which it passes. As for the agents attempting to establish identification all along the line as an original basis, not only does time not permit such procedure, our normal life span would not embrace it. Our fondest hope is that we do not fail too dismally.

"To go into the various transactions that tax the ingenuity of the examining officers, would serve no purpose at this point, as attempts have been made all through the schedules to cope with them as they appeared. Many have

- 2 -

probably been lost in the shuffle and will not again come to the surface, we hope. It is the intention of this explanation only to record for future ponderance in following this case forward the fact that all schedules and determinations were made at this time in accordance with the most logical interpretations which we could furnish or decipher from hieroglyphics encountered."

The Government has collected \$3,234,781.39 in the Associated Gas cases since October 1, 1934, but prior to the making of the jeopardy assessments in December 1935 for taxable years 1929 to 1933; \$1,014,000.00 of that amount was paid in 1935 on the filing of new consolidated returns pursuant to Commissioner's rulings on affiliations, as contrasted with original consolidated returns filed in 1929 and 1932, which showed no tax due.

Offers of settlement are now being considered by this office in respect to two cases for 1927 and 1928 against System companies in the aggregate amount of approximately \$300,000.00.

The investigation of the tax returns of substantially all the companies has been completed to and including the year 1934. There are presently employed about ten lawyers actively, and about ten others part-time, in addition to between thirty and forty agents, auditors and accountants.

2. District Court of the United States for the District of Delaware.

Eastern Utilities Investing Corporation is reorganizing under Section 77B of the Bankruptcy Act, but the value of the total assets which it declared was greatly less than the amount of the tax claims. On January 10, 1938, this office, through the United States Attorney, filed a petition under Section 21a of the Bankruptcy Act alleging that the corporation had additional undisclosed assets in the form of causes of action against its former officers and directors who were also in control of the Associated Gas and Electric Company. The petition made allegations of mismanagement and improper transfers of assets to Associated Gas and Electric Company, which facts could only be disclosed by examining said persons and forcing the production of documents in the Bankruptcy proceeding. The petition was granted in April by the District Court and an appeal was taken to the Circuit Court of Appeals for the Third Circuit. On July 6, 1938, the Circuit Court affirmed the District Court and the examinations are now set to commence on November 10, 1938. Owing to the difficulty that usually prevails

- 3 -

in locating H. C. Hopson for subpoena service, this office upon learning that he was to testify before the Securities and Exchange Commission on October 10, 1938, promptly obtained and served a subpoena requiring him to appear at the 21a examinations.

The tax claims asserted against Eastern Utilities for the years 1933 to 1935 aggregating approximately \$3,000,000.00 were tried in September before the District Court and briefs are now being prepared. On October 7, 1938, the Board of Tax Appeals handed down its opinion in the 1927 and 1928 tax cases and sustained deficiencies against this corporation in the aggregate amount of \$110,000.00.

### 3. Securities and Exchange Commission.

On June 20, 1938, the Securities and Exchange Commission commenced public hearings in connection with its Investment Trust Study on Eastern Utilities Investing Corporation. This hearing was in large part actuated by this office at a time when it was doubtful whether the District Court of Delaware would grant the Government's petition for the 21a examinations. It was deemed desirable to have as many of the facts concerning mismanagement made a matter of public record so that if the 21a examinations were denied it would still have been possible for the trustee in bankruptcy to institute suits based on the evidence brought out by the Commission. Much of the information along these lines which the Commission was able to place in its public record through the testimony of the former officers was furnished by this office pursuant to formal request by the Chairman of the Commission. The Commission in turn, at the request of this office, has now made available its entire files relating to this corporation and valuable leads thereby obtained are being followed up.

### 4. Investigations in Canada.

H. C. Hopson owned and controlled four Newfoundland corporations which were used as the principal means of milking the Associated Gas and Electric Company System for his personal benefit. In 1934 a revenue agent requested permission to examine the books of these four companies. He was told that there would be a few days delay but that the books would be produced as soon as possible. After the lapse of considerable time and the books failed to appear a revenue agent's subpoena was served and upon the continued failure to produce the books the matter was taken to the District Court for the Southern District of New York. The Government's position was sustained but the Circuit Court of Appeals reversed on the grounds that the books were in Canada and it had not been shown that they were under Hopson's control. It has since been learned that the books were moved to Canada after the agent had

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requested their submission and immediately upon their removal the corporations were placed in voluntary liquidation and a Canadian liquidator appointed. Canadian counsel for the liquidator filed in that proceeding affidavits to the effect that the books were in his possession but that he would refuse to allow their inspection.

It is impossible to overstate the relevancy and importance of these books in the 21a examinations, in the personal income tax cases against Hopson, and in the estate tax case against his mother. In them will be found the whole story involving millions of dollars improperly withdrawn from the System for the personal benefit of Hopson and his family. Owing to the fear that these books would be immediately destroyed upon the first overt act of the Government to obtain them in the 21a examinations, it was deemed desirable to take all preliminary steps in Canada to prevent their destruction prior to attempting to subpoena them in the 21a examinations. Since the above-mentioned affidavits stated that these books were in Halifax, Nova Scotia in 1934, representatives of this office went there secretly on September 26, 1938. The purpose of this trip was to devise a method for freezing the books in the hands of the present holder pending the completion of the legal steps necessary to examining them under a commission to take foreign testimony which will issue out of the Federal District Court of Delaware.

After conferring with the United States Consul and the Commissioner of Income Tax for Nova Scotia it was deemed necessary to employ counsel in Halifax for the purpose of assuring immediate action as soon as notified by this office. After investigation, the representatives of this office selected Mr. L. A. Lovett, K. C., and permission to retain him was procured by long distance call from Halifax to Assistant Attorney General Morris with whom the entire matter had been thoroughly discussed prior to the time the representatives of this office left for Canada.

As part of the plan to obtain these books the representatives then went to Ottawa where an appointment had been arranged through the American Legation for them to consult the Commissioner of Income Tax for the Dominion of Canada. It was believed that less suspicion would be aroused if the Canadian authorities ascertained the present whereabouts of the books. The Commissioner expressed his desire to cooperate in every way and after a short conference he became so interested that he requested permission to see the representatives in their hotel that evening. Accordingly a three hour conference at the hotel resulted during which the Government's problem was fully outlined and the Commissioner was further advised that the Newfoundland companies had paid no tax to the United States on the grounds that the transactions in question had taken place in Canada. When the Commissioner heard that no Canadian taxes had been paid he saw the possibility of obtaining substantial Canadian taxes by uncovering a gigantic fraud and was more than mildly



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enthusiastic in his offer to cooperate. He stated that if the books were in Canada he would not stop until he had procured them. He then said he had some doubt if the disclosure of this information to the American Government was permitted in view of the fact that the pending treaty has not been signed but that he intended to use this case to illustrate to the Canadian Government the importance of executing the treaty immediately. In this respect he felt that his efforts would be considerably aided if a little pressure could be exerted through our State Department. According to the Commissioner no one in the Canadian Government is opposed to the treaty but the matter has been allowed to lapse pending the negotiation of a similar treaty recently executed with France.

The Commissioner indicated that when he obtained the books a method would be found for informally advising the representatives of this office of this fact. Immediately thereafter a commission for foreign testimony will be obtained from the District Court of Delaware and efforts will be made to ascertain their contents.

5. District Court of the United States for the Northern District of New York.

Jeopardy assessments for taxes for the years 1927 to 1933 having been made, the Government brought a suit in equity to foreclose income tax liens and for receivership and incidental relief, which suit was instituted in the District Court of the United States for the Northern District of New York on March 2, 1936. After unsuccessful negotiations for a stipulation were terminated, an amended bill in equity was prepared but has never been filed. This amended bill alleged acts of mismanagement and financial manipulations and was intended to form the basis of an application for the appointment of a receiver.

6. Negotiations for settlement.

On June 22, 1938, a conference was granted to representatives of Associated Gas and Electric Company as a result of representations that they desired to arrive at specific terms on which all the tax cases against the System could be settled, and pending such settlement, the liens could be released. The terms laid down required the payment of \$2,500,000.00 cash, the placing of a similar amount in escrow, together with the giving of a bond or other acceptable security to assure the payment of all tax liabilities in excess of \$5,000,000.00.

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On July 18, 1938, representatives of Associated Gas and Electric Company advised me that it was impossible for them to raise \$5,000,000.00 and that \$750,000.00 was the maximum that could be raised within the System. After some discussion, I, with the approval of the Commissioner, stated that this placed the matter back where it was originally, that there was nothing presented to the Bureau in the way of a bona fide offer of settlement, and that until the taxpayer could make some offer which could be seriously considered there was no justification for further conferences. These negotiations, like all preceding attempts of settlement, were terminated when the Associated realized that it would be required to pay any substantial amount of cash.

7. Pending investigation on criminal prosecution.

In the last few weeks investigations have disclosed certain discrepancies with respect to four substantial items in the personal tax return of H. C. Hopson and one item in the estate tax of Hopson's mother, of which estate he is administrator and signed the return in that capacity. It is believed that these items are merely part of a general scheme which might ultimately prove sufficient to sustain an indictment for a conspiracy against Hopson, his brother-in-law, and certain officials of the Associated Gas and Electric Company. The investigation has not progressed to the point where it can as yet be stated that prosecution will be recommended. This matter is merely referred to so as you may be advised that it is being actively considered.

8. Application of Public Utility Holding Company Act.

On October 14, 1938, the Associated Gas advised the Securities and Exchange Commission that in compliance with its request plans and programs of integration and corporate simplification will be submitted before December 1st. The Holding Company Act confers on the Commission regulatory powers only and not the power of management. The financial set-up of the companies within the System is so complicated and confusing that there is a justifiable doubt if any regulatory body can control it effectively. The Treasury must be realistic in its dealings with this System and must not be content to rely on the announced pious intentions to comply with the Holding Company Act. I have seen too many instances of the present management paying lip service to the letter of the law and at the same time violating its spirit by wilfully creating situations of confusion which are impossible to penetrate. Should this policy of theoretical compliance but actual frustration be continued by the Hopson's interests, the Treasury must reconsider the question of vigorous pressing for the appointment of a receiver in the pending equity proceeding in the Northern District of New York. Otherwise the Associated Gas may render itself insolvent if, in fact, it is not already insolvent. In view of

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the practical difficulties, I recommend establishment of a unit to coordinate the activities of the Treasury and the Securities and Exchange Commission which will unify the policies of the two agencies and will serve as a clearing house for all information available to each. Only through close cooperation of this nature can there be any hope of keeping abreast of the constant shifts and changes within this System. This suggested coordination is essential pending final determination of the Government's policy of securing a change in the present management.

## TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE October 15, 1938.

TO Secretary Morgenthau

FROM Herman Oliphant

In re: Treasury aspects of Associated Gas and Electric System and Howard G. Hopson's personal companies.

Deficiencies have been asserted in forty-six cases against the System companies involving \$58,953,149.00, and in thirty-five cases involving \$6,568,493.00, against Hopson's personal companies. These cases are now pending before the Board of Tax Appeals. On October 7, 1938, the Board sustained deficiencies against Eastern Utilities Investing Corporation in the amount of \$110,000.00. The 1933 case against this corporation involving \$3,000,000.00 was tried before the District Court of Delaware this September and briefs are now in preparation. The task of preparing these cases for trial requires ten lawyers full-time, ten more part-time, and between thirty and forty agents and auditors.

In July 1938 the Circuit Court of Appeals affirmed an order permitting this office to examine the officers of Eastern Utilities in a pending 775 reorganization. The purpose of these examinations, now set for November 10, 1938, is to prove that this corporation has causes of action against its officers for mismanagement and improper transfers of its assets, and therefore has sufficient assets to pay its taxes.

In collecting the evidence for the examinations this office sent a representative to Halifax, Nova Scotia in order to obtain certain books of personal companies owned by Hopson. By permission of the Department of Justice, Canadian counsel was employed and the cooperation of the Commissioner of Income Tax of Canada was solicited. The Commissioner was enthusiastic in his offer of cooperation when he heard of the possibility of exposing a gigantic tax fraud perpetrated on the Canadian Government.

In June 1938 the Associated Gas representatives requested a conference with me on the allegation that they wished to settle and pay all the tax claims and to obtain a release of the tax liens. Terms were stated which required the payment of cash and posting security pending final settlement. These negotiations, like all preceding attempts of settlement, immediately came to nothing when the Associated Gas is required to pay over any cash.

Certain discrepancies in Hopson's personal companies' tax returns and those of his mother's estate, of which he is administrator, have recently prompted investigations with a view to criminal prosecution.

- 2 -

On October 14, 1938, Associated Gas advised the Securities and Exchange Commission that it would file before December 1st plans for integration under the Public Utility Holding Company Act. Whether the powers conferred on the Commission, which are purely regulatory, are sufficient to prevent the abuses in management now existing is somewhat questionable. In order that the activities of the Treasury and the Commission in this matter may be combined, I have suggested establishment of even closer contact in order that information may be mutually exchanged.

If more details are desired, a fuller memorandum containing them is attached.

Herman Oliphant

I have read this over the telephone to Mr. Oliphant and he has asked me to sign his name hereto.

Lyons Odum Jr

*(to H. Shih)* Copy for Mr. K.P. Chen  
*H. Shih*  
TRANSLATION OF CABLE FROM CHENPULAI dated October 15, 1938; 65

Strictly Confidential:

I am instructed to cable you the following:

- "1) Japanese invasion into Kwangtung undoubtedly aims not only at cutting our lines of communication and transportation of supplies, but also at severing China from contact and relation with the outside nations so that China may be brought under the military and political domination of Japan. The significance of this move is therefore very great in the general situation of the Far East.
- "2) As to our ability to carry on a long war of resistance, there is no serious difficulty as far as man-power is concerned, and we still have a quantity of munitions, which, if sparingly used, may enable us to fight on for some time. But our national finance is most urgently in need of help. We must have enough money to last at least a year before we can feel secure. It is sincerely hoped that American aid in this direction may come soon ~~so~~ so that it may not lose its time value.
- "3) Since the start of the South China campaign by the enemy, our whole plan of the war has to be reconsidered. The Wu-han cities will lose much of their importance, and will be defended 'passively'. The centre of the war is now shifted to the Canton-Hankow Railway.
- "4) With regard to the Wu-han cities, our plan is to pay not so much attention to the central objectives as to the preparations and positions on the periphery.
- "5) At this time, if the American Government could take the initiative to invite Great Britain to participate in some move for a more general solution of the Far Eastern Problem, there might be some chance of success. If America takes the lead, in all probability Great Britain will follow. Tell the American Government that China has every confidence in the leaders of the American Government. "

*Read by F.H.K.  
on Oct. 18, 1938 at Hyde Park*

WASHINGTON, D. C.  
October 17, 1938

MEMORANDUM

In connection with the woodoil proposition we have taken the following steps during our sojourn in New York City:-

1. The transportation problem in connection with maintaining a continuous flow of woodoil from interior of China to sea ports and of gasoline and other oils from sea ports to interior has been thoroughly discussed and solution found.
2. On the basis of the above discussion bids for motor trucks and servicing equipment have been received from the automobile factories represented at the meeting for trucks and equipment sufficient to maintain a continuous flow of woodoil at a rate of 100 tons a day via the three alternative routes already outlined.
3. Consultations have been held with Mr. Lawrence Morris and his associates in connection with formation of the proposed American Corporation. In accordance with their recommendations we have authorized them to proceed with the incorporation in the State of New York with tentative corporate name and nominal directors.
4. We have also asked them to prepare two draft agreements on woodoil which may be used as basis for future discussions.

One agreement between a Chinese Government agency and the new Corporation in formation for the sale of 5 years' supply of woodoil at an agreed price. The price will consist of two parts: One part represents fair average market price which is not subject to change unless condition of supply and consumption necessitates it, and another part represents contingent cost due to war conditions which will be subject to revision according to changing transportation costs.

Another agreement is to be between the new Corporation and a syndicate of consumers and/or importers for the sale of similar quantity of woodoil and at similar prices but on slightly different terms as to delivery etc. The total quantity involved is tentatively set at 350,000 short tons to be delivered as per the following schedule:-

1st year	50,000 tons
2nd year	60,000 "
3rd year	70,000 "
4th year	80,000 "
5th year	90,000 "

The incorporation papers and the draft agreements will be ready by Wednesday, the 19th instant.

In order to expedite the matter, authority and appropriation of US\$2,000,000 have been obtained from the Chinese Government to purchase trucks and other equipment. We are proceeding with the purchase with dispatch.

For your information our Government has authorized the Foreign Trade Commission to buy up all available stock at the woodoil trading centers and ship it to U.S.A. as quickly as possible. The first shipment of 730 tons have been made from Hongkong and 2500 tons are awaiting shipment at the same port. Shipments from interior centers are being expedited.



CABLE RECEIVED FROM CHUNGKING

Dated Chungking, October 15, 1938  
Recd. Wash., D.C. October 15, 1938

FROM: DR. H. H. KUNG  
TO: MR. K. P. CHEN

Confidential Referring to your telegram No.12

I appreciate Secretary Morgenthau's suggestion of appropriating US\$ 2 million from silver proceeds for purchase of trucks and you have my authority to act accordingly.

KUNG

FEDERAL RESERVE BANK  
OF NEW YORK

October 15, 1938.

Dear Mr. Secretary:

There were no public offerings of new corporate security issues this week, but announcement was made of a previously arranged private sale, to three insurance companies, of \$40,000,000 Union Carbide and Carbon Corporation debenture 3s of 1953. Of the total, \$16,000,000 is to refund 3 1/2s of 1950, sold three years ago, and \$24,000,000 is for new capital. Two large, high-grade refunding issues for utility companies are expected next week.

Offerings of municipal securities this week were the largest in several months. Of the \$31,800,000 total, \$17,900,000 was the result of transactions involving the Reconstruction Finance Corporation. A syndicate offered to the public, and entirely sold, \$10,000,000 of Pennsylvania Turnpike revenue 3 3/4 per cent bonds of 1968. These bonds were part of an issue of \$35,000,000 bought by the Reconstruction Finance Corporation to finance, along with a Public Works Administration grant of \$26,000,000, a 162-mile toll highway between Harrisburg and Pittsburgh. The Corporation bought the entire issue at 91.57 and resold \$10,000,000 at 95 1/2; the dealers' syndicate reoffered them at 100, and the bonds are quoted in the market at a fractional premium.

The Corporation was also involved in an issue of \$7,900,000 City of Utica, New York, bonds issued to finance acquisition of the city's water works. The issue was sold to dealers and reoffered to the public. There were several other issues of over \$1,000,000, reception of which ranged from fair to very good.

The market would no doubt absorb larger amounts of high grade new issues, both corporate and municipal, than are being offered. The only restraint upon investment demand appears to be some feeling that interest rates will eventually rise appreciably, and that long-term issues bearing the interest rates now prevailing will then depreciate in price. This restraint is not very effective at the moment.

Yours faithfully,



Allan Sproul,  
First Vice President.

Hon. Henry Morgenthau, Jr.,  
Secretary of the Treasury,  
Treasury Department,  
Washington, D.C.

October 19, 1938.

Dear Mr. Spraul:

On behalf of the Secretary I am acknowledging your letter of October 15th. The information you sent is most helpful and is much appreciated.

Sincerely yours,

H. S. Klotz,  
Private Secretary.

Mr. Allan Spraul,  
First Vice President,  
Federal Reserve Bank of New York,  
New York, New York.

cc to HF

GKF/dbs



GENERAL COUNSEL  
TREASURY DEPARTMENT  
WASHINGTON

October 17, 1938

Dear Mr. Secretary:

As I said in our telephone conversation about your proposed talk with Mr. Gifford, I believe that your objective would best be served by discussing the matter with him from the broad moral and practical standpoint. The technical side could be disposed of, I should think, by <sup>saying you have</sup> (giving him) the attached copy of our memorandum on the subject and telling him that we are convinced that his company can validly refuse service to companies which sell racing information to bookmakers, but that the legal question is one for the lawyers to argue about, not you and him.

At the outset you should know that Mr. Gifford, as President of his company, has publicly expressed his distaste for the type of business represented by racing news services. The Nation of July 30, 1938 quotes him as having said at a Federal Communications Commission Hearing in 1936:

"We do not want to deal with people who are breaking the law, whether it is race horses or anything else, \* \* \* This is a messy part of our business. It is difficult because we are advised on one side that we cannot legally defend refusal to give service in many cases where it would be our inclination and desire to do so, having no right to discriminate on the ground of character between subscribers, while on the other hand the Attorney General of Rhode Island has expressed the view at these hearings that we should be guided in our decisions by the character of applicants . . . It seems to me that the matter is one for local law enforcement."

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I suggest the following general approach as the basis for your discussion with him:

1. The bookmaking evil has in recent years grown to staggering proportions. The sums involved have approached such magnitude as to make this illegal traffic one of the nation's greatest racketeering and crime factors. It has been estimated that well over a billion dollars changed hands illegally in this manner in 1937.

2. Mr. Gifford and you, as two good citizens, are primarily interested because bookmaking takes honest, potentially useful dollars and turns them into demoralizing, crooked profits.

3. But the Treasury has a special interest in the matter. The illegal bookmaking and gambling setup is the cluster point for illegal operations in other fields throughout the United States. Many of these are the Treasury's responsibility—narcotic peddling, counterfeiting, illicit liquor, etc.

4. Aside from your official interest, you, as a citizen, have a deep personal interest in the matter as a moral issue because you feel that it represents potentially as great a force for evil as did the bootlegging and racketeering of the Prohibition era. It is something in opposition to which public-spirited citizens must mould public opinion.

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5. In the statement quoted above, Mr. Gifford stated that he felt that the matter was one for local law enforcement. It is true that almost all of the 48 States have laws regulating or prohibiting wagering on horse races. However, because of the interstate character of the communication facilities, which makes this practice possible on a nation-wide scale, the States as a practical matter are helpless effectively to deal with the problem. If the evils of gambling on horse racing were confined to the States in which the races are actually run, then, the problem would be as simple as Mr. Gifford indicated. But the actual situation is that bookmaking is not confined to the fifteen horse racing States. On the contrary, because of the large scale use of "private wires" which cover the entire country like a great network, bookmaking today flourishes, a single national system in every State of the Union.

6. You feel, therefore, that the matter can only be dealt with uniformly on a national basis. The evil is, of course, one which could be curbed by legislation; but why legislation and more government to enforce if other cures are possible? In the meantime a bad situation is growing steadily worse. The racing news services would have to stop operating if the American Telephone and Telegraph refused them leased wire services. Without these news services, bookmaking could not continue as a nationwide racket.

7. The problem can be cured without legislation by Mr. Gifford. Therefore, you are asking for his immediate action.

8. Mr. Gifford has shown himself notably public spirited in the free tender of his services for many charitable, educational, and governmental purposes (Who's Who in America shows him to be on several college boards, including Harvard and Johns Hopkins; President of the Charity Organization Society of New York; Director of the President's organization on unemployment relief during the winters of 1931-2, etc.). If he should be responsible for the adoption of a new policy by his company which would result in leased wire service not being furnished to news agencies disseminating racing information to bookmakers, he would have performed a service of greater importance to the public than any of those for which his name is already known.

9. The Treasury's legal staff, after carefully looking into the matter, is satisfied that the Telephone Company can validly refuse its facilities in the circumstances indicated. Like so many others, the question is one on which able lawyers may reasonably differ, but the importance of the objective is too great to permit its achievement to be delayed or defeated by all the legal doubts ingenious lawyers can conjure up. Certainly since the issue is a moral one, the weight of public opinion <sup>would be on Mr. Gifford's side</sup> ~~will cause any doubt to be resolved in favor of~~ ~~legality.~~

Sincerely yours,

*Herman C. Crisp*  
General Counsel

The Honorable

The Secretary of the Treasury

Enclosure

NOV 3 1937

The Secretary

Herman Oliphant

This is a memorandum on the question as to whether the American Telephone and Telegraph Company can refuse leased-wire service to the Nation-Wide News Service, the principal purveyor of racing information to bookmakers.

Summary

It seems clear that if the American Telephone and Telegraph Company might legally refuse to give leased-wire service to the companies who sell racing information to bookmakers, these news companies could not continue to do business. In turn, the continued existence of the large-scale bookmaking business is dependent upon the news companies because it cannot operate without receiving racing news almost instantaneously from the track.

In inquiring as to whether the American Telephone and Telegraph Company could refuse service to the Nation-Wide News Service, we were immediately confronted with the Federal law which requires the Telephone Company to give service to anyone who applies for it and is willing to pay the company's reasonable rates and comply with its reasonable regulations. This law is subject to the well-established exception, however, that no utility will be compelled to give service to be used for an illegal purpose.

Consequently, it was necessary for us to determine whether, in view of this exception to the general rule, the American Telephone and Telegraph



Company might refuse service to the Nation-Wide News Service if it were established that the latter company was regularly transmitting information through the Telephone Company's facilities to illegal bookmaking establishments and that this fact was known or ought reasonably to have been known to the American Telephone and Telegraph Company.

We have concluded that the Telephone Company may, under these circumstances, justify a refusal of private-wire service to the news company. The authorities on this question indicate that, if the news company sells exclusively to illegal enterprises, the Telephone Company may refuse service forthwith, but that, if the news company caters to legitimate newspapers and racing sheets as well as illegal business, the news company must be given an opportunity to cease selling its news to illegal enterprises before telephone or telegraph service may be refused. The Telephone Company may give the news company this opportunity to mend its ways by promulgating a general regulation to the effect that, if leased-wire service is put to illegal uses, the service will be discontinued notwithstanding any contract existing between the parties. The judicial decisions indicate that such a regulation would be valid and would justify service discontinuance if violated.

The American Telephone and Telegraph Company in furnishing its facilities for the dissemination of sporting information is acting as a common carrier in interstate commerce and is therefore subject to section 201 of the Communications Act of 1934, 48 Stat. 1070 (U.S.C. title 47, sec. 201), which requires all common carriers and public utilities to furnish their

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services to all alike without discrimination. Matter of Private Wire Contracts, 30 I. C. C. 751, 751, 759; Eastern Union Telegraph Co. v. Foster, 247 U. S. 105. However, this general rule against discrimination is subject to the exception that service may be refused or withdrawn if it is being used for illegal purposes. The judicial decisions which have enunciated this exception would justify the refusal by the Telephone Company to give service to the Nation-Wide News Service.

Smith v. Eastern Union Telegraph Co., (1887) 84 Ky. 604, 2 S.W. 465, presents a good example of the manner in which courts deal with cases of the character under consideration.<sup>1</sup> The petitioner, the owner of a bucket shop, filed a petition for mandamus against the Telegraph Company to require that

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<sup>1</sup>Other cases identical in principle to the Smith case follows

People ex rel Niegel v. New York Telephone Co., (1922) 195 N.Y. Supp. 552, (refusal of telephone service to a bookmaker);

Thurston v. Union Pac. R. Co., (1877) 25 Fed. Cas. 1192, (refusal of railway service to one who intended to gamble on the train);

People ex rel Montario v. New York Telephone Co., (1917) 167 N. Y. Supp. 1114, (refusal of telephone service to a bookmaker);

Eastern Union Tel. Co. v. State, (1905) 165 Ind. 492, 76 N.E. 100 (refusal of telegraph service to a bucket shop);

Sullivan v. Postal Tel. Cable Co., (C.C.A. 7th, 1905) 125 Fed. 411 (refusal of telegraph service to a bucket shop);

People ex rel Eastmeyer v. New York Telephone Co., (1918) 159 N. Y. Supp. 369, (refusal of telephone service to a bookmaker);

Gullen v. New York Telephone Co., (1905) 94 N. Y. Supp. 290, (refusal of telephone service to a bookmaker);

Godwin v. Carolina Tel. & Tel. Co., (1904) 138 N. C. 255, 48 S. E. 635, (refusal of telephone service to a house of prostitution);

Arrant v. Eastern Union Tel. Co., (C.C., S. Ky., 1885) 17 Fed. 825, (refusal of telegraph service to a bucket shop).

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Company to furnish him with the use of telegraph facilities for the reception of market reports, and contended that the Company was under a duty to give service notwithstanding the character of the patron's business. The court held that the Telegraph Company could not be compelled to render a service which was indispensable to the continued existence of a business which was contrary to law, good morals, and public policy.

There is an apparent distinction between the Smith case and the situation under discussion, for in our case the bookmaker, conducting an illegal business, is not the patron of the Telephone Company and would not be seeking the telephone service. On the contrary, the Nation-Wide News Service, engaged in a business which is not made illegal by statute, is the patron and would be seeking the service. It is because of this distinction that the American Telephone and Telegraph Company has taken the position that it has no legal right to refuse service to the news company. It contends that the Smith case and others of its kind do not justify the Company in going behind the news company to question the legality of the business in which the purchasers of the information are engaged.

It is believed that the Telephone Company places too narrow a construction upon the cases. The principle upon which they are based is that a public utility should not be compelled to foster an illegal enterprise. It is difficult to believe that a court would ignore the patent fact that, if it compels service to the news company, it would, as a practical matter, be compelling service to bookmakers. No decisions were found which would throw any doubt upon the validity of this proposition, and the lower court cases, which are closely in point, may be cited to support it.

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In People ex rel Sleight News Co. v. New York Telephone Co. (N. Y. Sup. Ct., Special Term, N. Y. L. J., December 17, 1918), the petitioner was a concern engaged in disseminating sporting news and it was shown upon the trial that violations of the bookmaking statute resulted from the dissemination of this information. The court refused to grant a writ of mandamus. Again in People ex rel Empire News Co., Inc., v. New York Telephone Co. (N. Y. Sup. Ct., Special Term, N. Y. L. J., March 10, 1919), the petitioner was a news company, but it appeared from the evidence that the company furnished information to legitimate newspapers as well as to bookmakers. The court granted the writ of mandamus upon the condition that the petitioner restrict its sales to legitimate enterprises. These cases appear to be supported by the decisions in the Smith case and others of its kind and would afford a sound legal basis for the refusal by the American Telephone and Telegraph Company to give service to the Nation-Wide News Service.

As above stated, the court in the Empire News Company case granted the writ of mandamus because the news company was able to show that it catered to legitimate newspapers, but granted it only upon condition that the news company restrict its sales to such legitimate enterprises. Since it is possible that the Nation-Wide News Service does business with legitimate enterprises as well as bookmakers, it is necessary to take cognizance of this element in the Empire News decision. Since a violation of the court's order in that case would have entitled the Telephone Company to refuse leased-wire service, the effect of the decision is merely to give the news company an opportunity to mend its ways before denying it telephone service.

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If it appears that the Nation-Wide News Service does sell news to some legitimate establishments, it is believed that the Telephone Company could give the News Service the opportunity, apparently required by the Empire News decision, to sever its connection with illegal enterprises by issuing a general regulation to the effect that leased-wire service would be discontinued if put to illegal uses. It is well settled that a public utility can refuse or withdraw service if the patron fails or refuses to comply with its reasonable regulations<sup>1</sup>. The criterion that determines the validity of a public utility regulation is its reasonableness as judged upon the facts and circumstances involved in the particular case. For example, utilities may promulgate and enforce regulations designed to protect their equipment<sup>2</sup>, to eliminate waste of their particular product<sup>3</sup>, to protect the public from injury from use of their equipment<sup>4</sup>, to insure the payment of their charges<sup>5</sup>, and to foster the efficiency of their service<sup>6</sup>. Certainly, it would seem that, if a court may properly lay down a rule, as was done in the Empire News case, to the effect that service could be discontinued if put to illegal uses, a regulation issued by the Telephone Company to the same effect would be held valid. After the promulgation of such a regulation, the Company could immediately discontinue leased-wire service with impunity, if the Telephone Company discovers that the News Service

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1. Harbison v. Knoxville Water Co., (1899) 55 S. W. 995.
  2. Gardner v. Providence Tel. Co., (1901) 48 Atl. 1004.
  3. Shiras v. Ewing, (1892) 29 Pac. 520.
  4. Hiegard v. Alabama Power Co., (1930) 127 So. 206.
  5. Western Union Tel. Co. v. McGuire, (1886) 2 N. E. 201.
  6. Huffman v. Mary Mutual Tel. Co., (1908) 121 N. W. 1035.

continues to violate its regulation by using the leased wires to foster book-making establishments.

It should be stated in this connection that an examination of the American Telephone and Telegraph Company's regulations governing private-wire service failed to reveal the existence of any such general regulation as is above suggested. We understand, however, that the Telephone Company does, at the present time, insert a provision in their contracts with the Nation-Wide News Service to the effect that, if the Company is advised by a local prosecutor or other law officer that their equipment is being used for illegal purposes, they will remove the equipment and discontinue service. This is obviously not broad enough to accomplish the purpose desired, for, in the first place, the Telephone Company has, in accordance with the contract provision, abstained from acting until they are requested to do so by the local prosecutor, and, in the second place, the provision would permit discontinuance of service only for the particular bookmaking establishment and not for the entire Nation-Wide News Service net work.

file 10-17-38.

Return to Room 2592

October 25, 1938.

Dear Randolph:

Thank you very much for your letter of October 17th. I was glad to have the material you sent me in so much detail, and also your comments on the meeting at Chicago.

Sincerely,

Henry

Airmail-

Dr. W. Randolph Burgess,  
The National City Bank of New York,  
New York, New York.

P.S. I would appreciate it if you would write to me again in order that I may have the same type of information this coming Monday.

GWF/dbs

cc to H/S

Thank him for this letter *NY*

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*The National City Bank*  
*of New York*  
ESTABLISHED 1818

Return to Room 236

*New York* October 17, 1958

CABLE ADDRESS 'CITYBANK'

IN REPLYING PLEASE QUOTE INITIALS

Dear Henry:

Your note of last week only reached me this morning because I spent Friday and Saturday in Chicago at the meeting of the Reserve City Bankers.

During the past week there were no offerings to the public of any corporate issues of any size, though there were reported a number of direct sales to life insurance companies, including \$40,000,000 Union Carbide debenture 5s due in 1953, which were sold to three insurance companies in September, apparently. Two other smaller issues likewise sold to insurance companies were \$8,500,000 Washington Gas and Light Company 4s of 1963, sold at 101 to six insurance companies, and \$2,100,000 Mississippi Valley Public Service Company First 4s of 1965, sold to two insurance companies at 101 1/2.

In municipals, \$7,900,000 of Utica, New York, Water Revenue Bonds 2 to 35 years, were sold to the R. F. C. and reoffered, but moved rather slowly. In addition \$10,000,000 of Pennsylvania Turnpike 50 year bonds sold to the R. F. C. at 95 3/4 and reoffered at par, appear to have been well distributed.

During the next ten days a number of large issues are expected, and the market appears to be in shape to take them readily. These issues include the following:

October 19 - \$80,000,000 Public Service Co. of Nor. Ill  
First 5 1/2s due 1968. The price will probably be 105.



This marks another step in the great refunding operation of the Commonwealth Edison System. The indications are that the issue will be an immediate success.

October 20 - \$55,000,000 Ohio Power Co. First 5 1/4s due 1968. This is another piece of refunding and indications are that it will also go exceptionally well. Price not yet fixed. Will probably be between 101 and 102.

October 25 - \$50,000,000 Firestone Tire & Rubber Co. 3 1/2% Debentures due 1948. This piece of financing will be used largely to clean up current bank loans and will put the company in exceptionally fine position. Price has not yet been fixed, but will probably be slightly under 100. The insurance companies have shown real interest in the business and, because of the attractive maturity (10 years) it will be well received by banks.

October 25 - \$55,000,000 Wisconsin Electric Power Co. First 3 1/2s due 1968.

\$14,500,000 Wisconsin Electric Power Co. 10-Year Serial Notes.

Price not yet fixed. Long bonds will probably be issued at 103. The serial notes will be taken by a group of banks, including National City Bank. The average rate on the notes will be 3.40. The long bonds are top-grade and should be absorbed immediately.

Generally speaking, the market is in fine shape, with extremely little securities on the shelves.

As you may know, the banks here are now very much interested in making term loans to corporations; that is, loans with maturity of 5 or even 10 years. A number of the banks are reluctant to go over 5 years, and we ourselves have very few beyond that maturity, but some as long as 10 years are being made, and we are participating in two or three.

The Reserve City Bankers, whose meeting I attended in Chicago, have been doing a lot of work on this question, and I think it is fair to say that the banks which they represent are making a real try at putting their money to work in this way, although, of course, the amount of such loans that can be made is relatively limited. Generally speaking, business

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is not looking for new money in large amounts.

Jesse Jones attended the meeting for two days, and had a very frank and goodnatured discussion with those present. I think it was helpful in getting a mutual understanding.

Sincerely yours,

*William C. Clegg*

Honorable Henry Morgenthau, Jr.,  
Secretary of the Treasury,  
Washington, D. C.

WRB.H

TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

CONFIDENTIAL

DATE October 17, 1938

TO: Secretary Morgenthau  
FROM: Mr. Haas *HAAS*  
Subject: The Business Situation,  
Week ending October 15, 1938

Conclusions

(1)

As business activity approaches its seasonal November peak, it is being aided by increased confidence growing out of the various evidences of improving business, notably by the rise in stock prices to new high levels and by a sharp upturn in steel activity.

(2)

A weakening in finished steel prices this week, including a reduction of \$4 or more a ton on automobile steel, follows a pattern characteristic of the early stages of a business recovery. The reduction has stimulated steel buying by the automobile companies, and seems likely to prove beneficial to general business.

(3)

Renewed weakness in foreign currencies, however, cloud the longer business outlook, indicating continued pressure from abroad on commodity prices. While increased speculative interest, a stronger industrial demand, and decreased supplies for many commodities favor a rising price trend, commodity prices on the whole have been unable to make much headway against the influence of the weak foreign situation.

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The general picture

Business activity currently shows an improving trend, which under favorable conditions may develop into a sustained recovery. The rise in stock prices this week to new high levels points in that direction, since it tends both to reflect a strong confidence in the business outlook and to generate further confidence. A sharp upturn in steel activity to above 50 per cent of capacity for the first time since last October, and other evidences of improving business, have also encouraged a general belief in higher levels yet to come. This is always an important factor in stimulating new buying, and thereby giving business activity the additional momentum needed to carry it forward.

The September FRB index (preliminary) shows a gain of 3 points over the August figure, reaching 91. While cotton consumption showed an unseasonal decline during the month, this was more than offset by a marked gain in steel activity and improvement in other industries.

Despite this current evidence of business improvement, however, the longer outlook is not entirely clear, chiefly because of continued weakness in the foreign situation and an unsatisfactory trend of commodity prices. Sterling exchange this week has shown pronounced weakness (See Chart 1), dropping back nearly to the low levels reached on the most critical days of the Czechoslovakian crisis, and the franc likewise. This appears to indicate continued deflationary pressure on commodity prices in this country. Several influences operating to raise prices -- increased speculative interest, rising industrial demand, and reduced supplies -- have been largely ineffective in overcoming this pressure from abroad, except for a few commodities.

The significance of the commodity price trend in the business outlook lies in its three-way influence on business activity: (1) through its effect on the volume of forward buying; (2) through its effect on the incomes of farmers and other producers of raw materials; and (3) through its effect on manufacturers' profit margins. Until the price situation begins to appear more favorable, the business outlook must continue to be viewed with some degree of caution, particularly since industry has not yet built up a normal backlog of unfilled orders to act as a cushion against temporary disturbances.

Secretary Morgenthau - 3

Commodity prices

Prices of individual sensitive commodities in recent weeks have shown diverging trends, with the net result that average price indexes have tended to move sidewise, instead of showing the strong rising trend that should normally be under way at this stage of the business cycle. Agricultural prices as a group have declined, while prices of a number of industrial raw materials have risen. Movements of the several indexes of sensitive prices have been affected to some extent by the particular commodities included, and by their respective weightings. This explains why the Dow-Jones futures index (shown in Chart 1) has tended upward during the past ten days, while Moody's index has declined to its September low. The BLS all-commodities index, after reaching 78.4 during the week ended September 24, has sagged back to 77.8 during the week ended October 8. This compares with the year's low of 77.4 reached in August.

Commodities which have shown greatest strength during the past few weeks have been chiefly industrial raw materials, particularly those which have been aided by marked improvement in supply situations. The rise in the price of copper to 11½ cents from the summer low of 9 cents has been accompanied by a decline in refined copper stocks to 315,191 tons on September 1, which compares with a 1938 high of 369,809 tons on June 1, prior to production curtailment by major producers.

Prices of tin and zinc have also been strong, partly reflecting a decline in U. S. stocks of tin on October 1 to 4,573 tons, as compared with a high of 6,385 tons on January 1, and a decline in U. S. stocks of slab zinc to 130,743 tons on October 1, as compared with the year's high of 149,671 tons on June 30. A sustained rise in hide prices has followed a decline in total U. S. stocks to 13,910,000 pieces on August 1, which compares with the year's high of 15,407,000 pieces on February 1.

Steel scrap prices, ordinarily considered an important guide to the trend of steel activity, have failed to follow the recent rise in prices of other metals and the upward trend in steel operations over the past several weeks (see Chart 2).

Viewed as a whole, commodity prices have reflected little of the improvement in speculative interest and business confidence suggested by the strong upturn in the stock market, nor of the revival in industrial demand which

has accompanied the marked increase in factory output. Deflationary influences in the price situation are apparently preventing the normal response of commodity prices to these constructive developments.

#### The steel situation

Operations in the steel industry showed a greater than seasonal increase this week to 51.4 per cent of capacity, the highest rate since the week of October 25, 1937. New orders likewise increased, the U. S. Steel Corporation report showing new orders for the week at the equivalent of 52 per cent of capacity, which compares with 42 per cent and 53 per cent in the two previous weeks.

A feature of the week was a general reduction of \$4 a ton on several important types of automobile steel in the Detroit area, with additional price concessions reported but not officially confirmed, precipitated by competition for an order of 25,000 tons or more from the Ford Motor Company. By the end of the week the weakness in steel prices had spread to other steel products and to all producing districts.

A decline in finished steel prices is characteristic of the early stages of a business recovery, since at such times, with large actual orders in sight, individual companies are willing to make concessions in order to increase their volume of business. As shown in Chart 3, steel prices weakened after the beginning of the recoveries in late 1921 and in late 1924, also at the beginning of the renewed advances in steel operations in early 1928 and early 1936.

In many quarters the present weakness is regarded as temporary, which is reported to have greatly increased the volume of steel orders from the automobile industry this week. The reduction in steel prices may therefore prove a definite stimulus to the steel industry and to business in general.

#### The automobile outlook

The weakness in prices of steel used by the automobile industry may raise the question whether the automobile outlook is as strong as recent trade reports have pictured it. The demand for steel from the automobile companies, even at this advanced stage in the production of new models, has evidently not been strong enough to maintain steel prices at the levels to which they had been reduced a few months ago. The steel companies may have been obliged to cut prices in order to move inventories of automobile steel which they had built up in recent months in anticipation of a strong fall demand, which so far has not materialized to the extent expected.

Secretary Morgenthau - 5

Automobile output this week continued its sharp seasonal rise, with an estimated output of 50,500 units, as compared with 37,700 units the week previous, and with 89,700 units in the corresponding week last year. The increases in the past two weeks have been at approximately the same rates as last year, but last year the output after this date held nearly constant for three weeks and then turned downward.

Dealer orders for the new models are reported to be very heavy, though there is some suspicion in the trade that dealers are increasing their shipping requests beyond their actual needs in order to insure delivery of the desired quotas. It is also thought that dealers may be over-optimistic in forecasting buyer demand, or wish to build up inventories in fear of labor troubles.

A Detroit analyst with special ability in the automobile field says that "logically the automobile situation points to relatively good sales for two to three months after the new model introduction, and then a somewhat slower period until general business picks up further". In support of the latter opinion he mentions, among other reasons, that the stock of cars in the hands of normal new car buyers is still fairly good, and that customers are not likely to come into the market heavily for some time to come, particularly the farmers and factory workers. He also raises the question whether the sharp improvement in residential construction, particularly of homes for the man with a steady income, may not take out a section of the usual new car market next year.

#### Further gains in construction

Residential construction continued to gain substantially during September, according to the F. W. Dodge reports, the month showing an increase in contract awards of 52 per cent over September last year. The daily average was somewhat higher than in August, whereas usually there is a seasonal decline. Two large housing projects in New York City, one of them the first unit of the huge Metropolitan Life Insurance Company project, accounted for more than half of the increase over September 1937.

There has as yet been no seasonal let-up in the volume of applications for insurance under the FHA, the amount of mortgages selected for appraisal continuing through September at the rate of \$22,000,000 a week established last March. This suggests a continued heavy volume of contract awards during the fall months,

since our studies show a definite two-month lag between the volume of mortgages selected for appraisal and the volume of residential contract awards. Some of the actual construction will doubtless be held over until next year, and constitute a backlog of business for the spring season.

#### New orders well maintained

Business activity continues to be supported by a well-maintained level of new orders during the early part of October, as shown by our weekly index (See Chart 4). An increase in steel orders has been the principal feature of the past week, and further advances are expected in coming weeks as a result of increased buying from the automobile companies. Recent newspaper reports that new orders of the American Radiator Company are "the heaviest in five years" are not borne out by our reports from the company, which show a seasonal increase for several weeks up to October 13, but with all weeks substantially below last year's order levels.

#### Recovery in durable goods

The recent improvement in industrial production has been shared almost equally by durable and non-durable goods, contrary to experience in the upturns of 1921 and 1932, when non-durable goods improved sooner and more rapidly. (See Chart 5.)

The ratio of the production of durable goods to the production of non-durable goods (shown in red in the upper part of Chart 5) is used by some economists to detect conditions of disequilibrium in industrial production. From the experience of the past 19 years, it will be noted that the extreme high and low points in the ratio have indicated major turning points in business activity. Owing to a tendency for non-durable goods to form a gradually increasing proportion of total industrial production, the significant points on the ratio have declined gradually, as indicated by the broken red lines.

Business activity in 1938 has turned upward without the ratio of durable to non-durable goods production reaching the lower limit of the ratios, somewhat as it did after the temporary recessions in 1924 and 1927.

#### The current business trend

The New York Times index of business activity for the week ended October 8 rose to 85.1, from 84.2 the week previous. The week was featured by a sharp rise in the automobile



Secretary Morgenthau - 7

production index. Steel production, lumber production, and "all other" carloadings showed somewhat greater than seasonal gains, while miscellaneous carloadings and cotton mill activity showed contra-seasonal declines.

The downward tendency in cotton mill activity since the middle of August was confirmed by the Census Bureau figures on cotton consumption for September, released this week, which showed 534,000 bales of cotton consumed by mills during the month, a reduction of 27,000 bales from the August figure. Normally there should have been an increase.

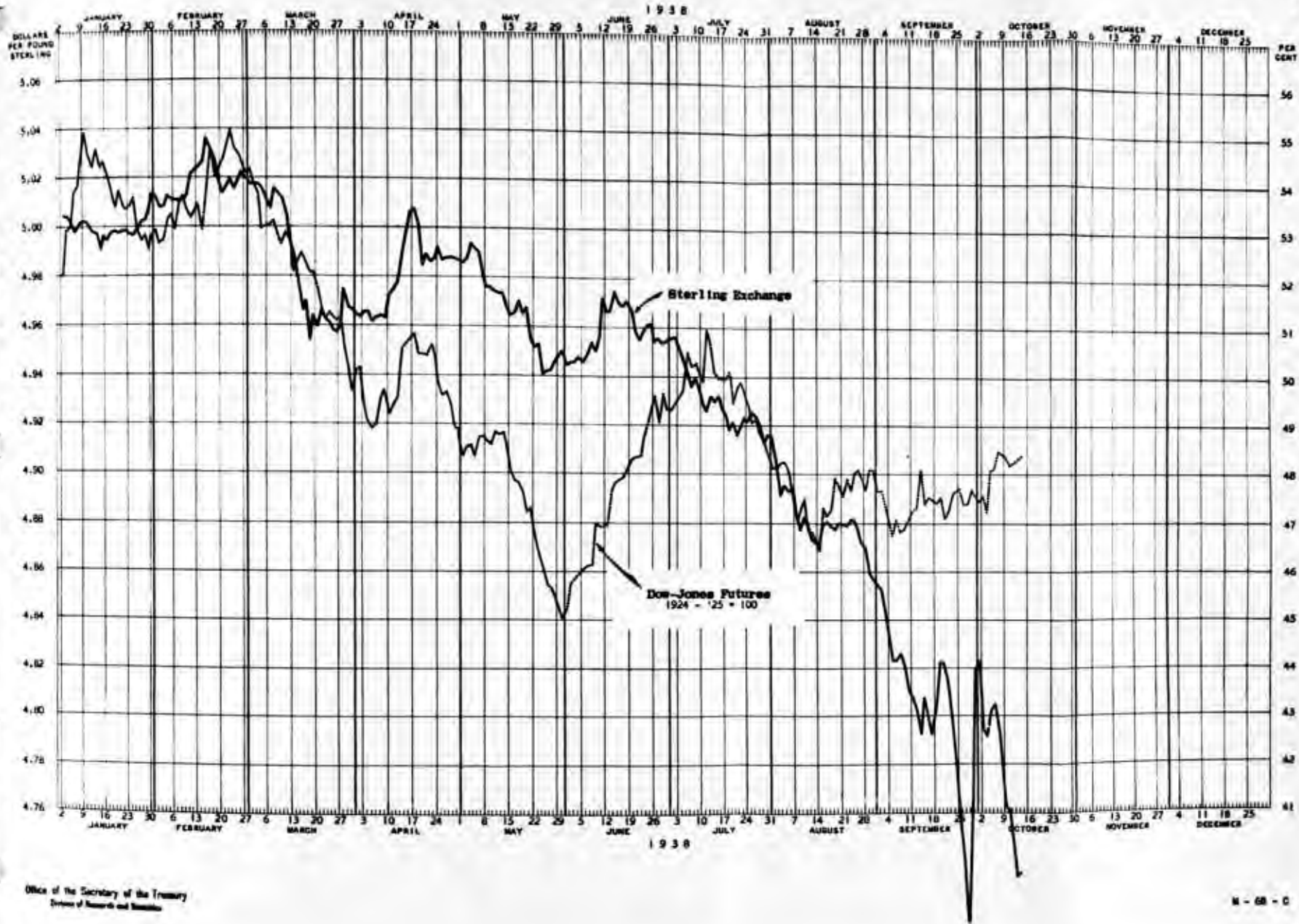
The reduced cotton mill activity has been due to a piling up of finished goods stocks at mills, according to trade reports. Retail stocks of cotton goods are reported to be reasonably low, although the FRB dollar value adjusted index of department store stocks (largely made up of textile products), when adjusted for price changes, is not much below that of last January. An index of 75 in July and August compares with an index of 77 in the months of January to March.

Department store sales for the week ended October 8 were 7.6 per cent below sales of the same stores during the corresponding week last year, comparing with a decline of 15.2 per cent the previous week.

STERLING EXCHANGE AND PRICES OF COMMODITY FUTURES

Chart 1

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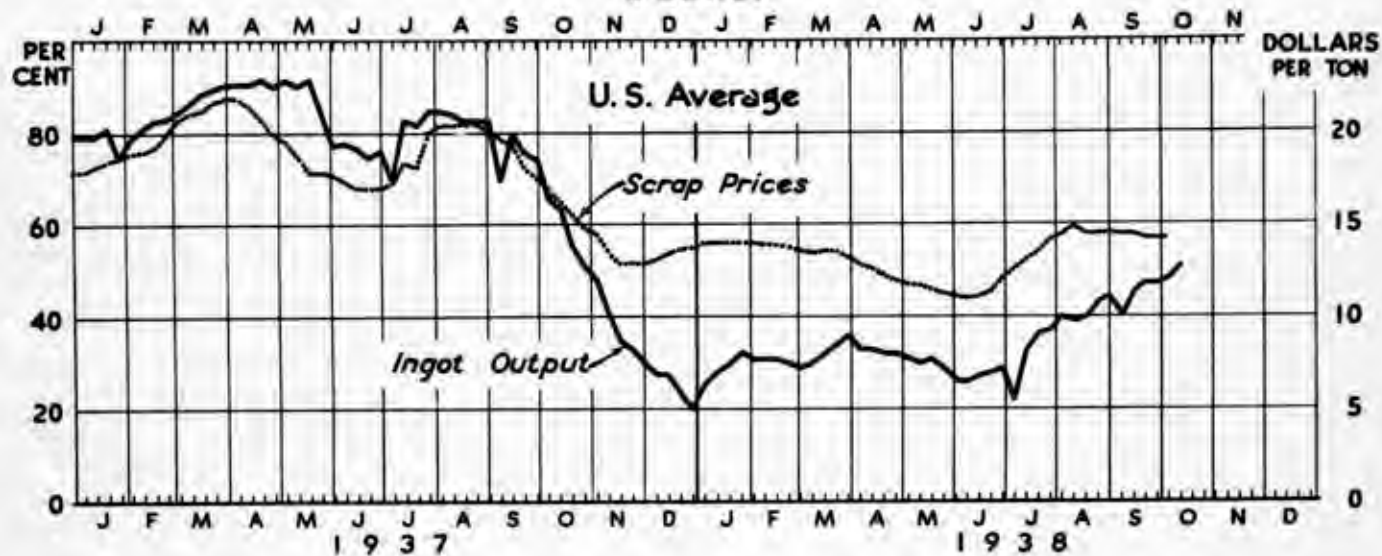


Office of the Secretary of the Treasury  
Division of Research and Statistics

M - 68 - C

# STEEL OUTPUT AND SCRAP PRICES

## Ingot Output in Percent Capacity WEEKLY

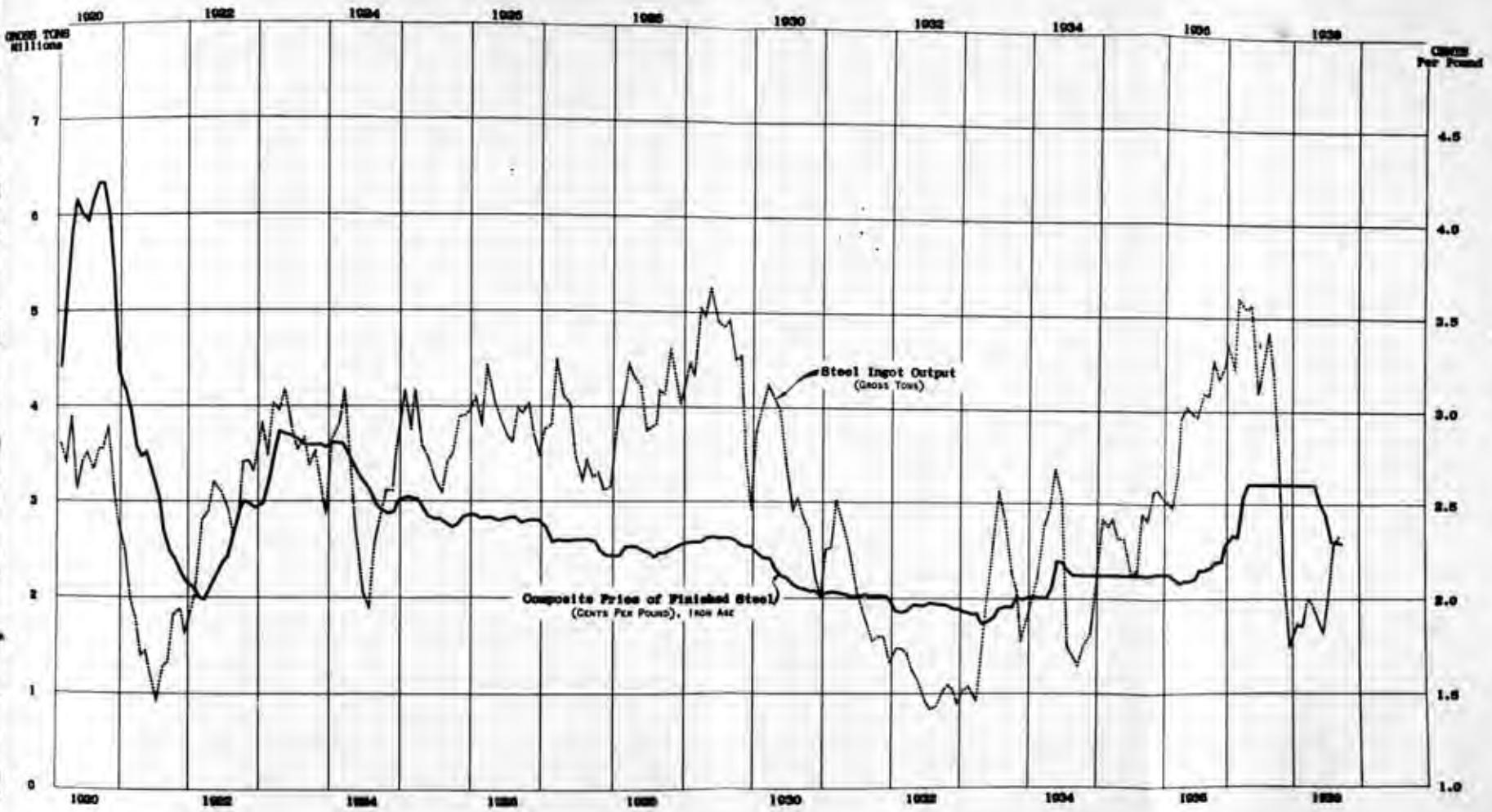


Office of the Secretary of the Treasury  
Division of Research and Statistics

C-190

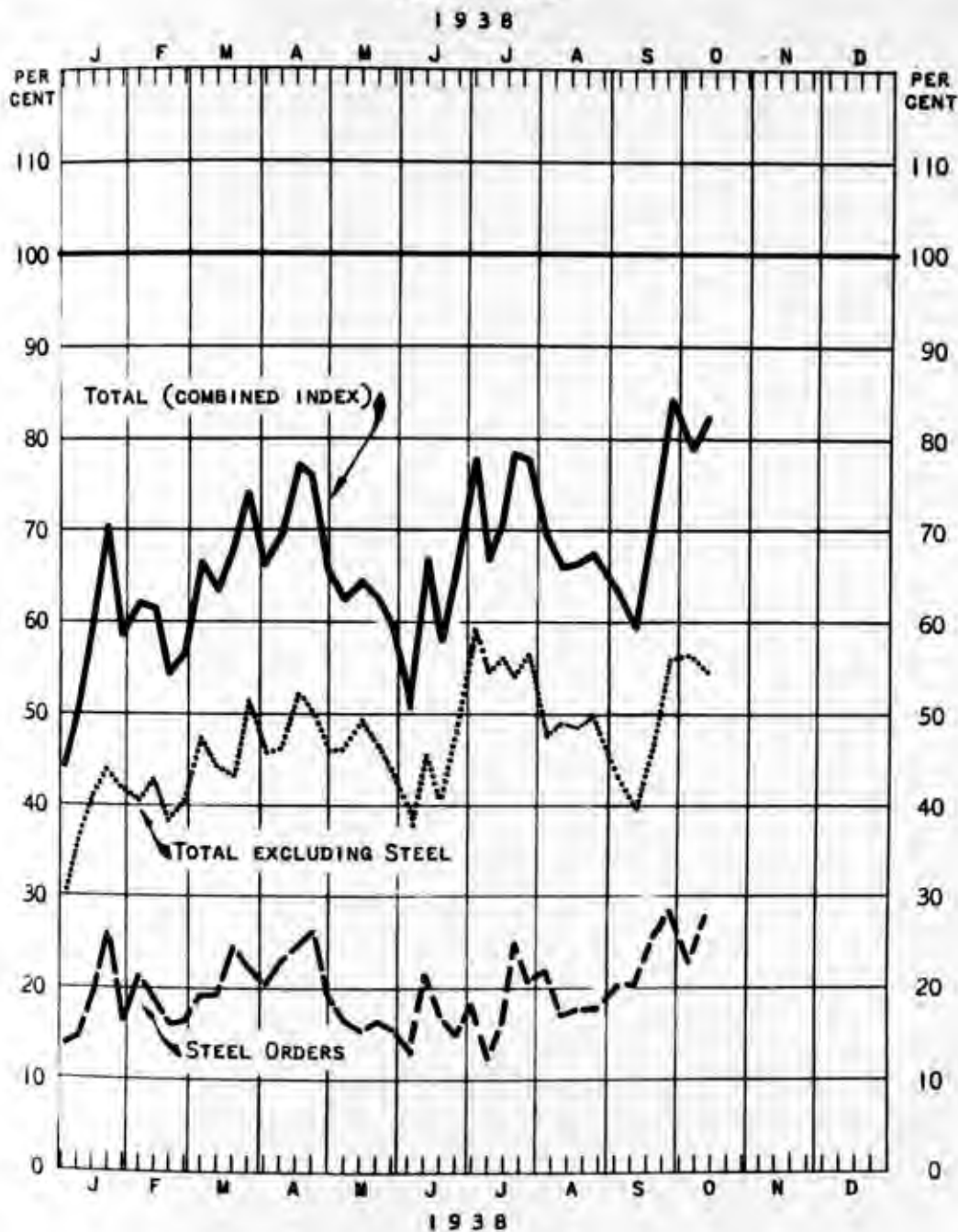
Chart 2  
94

### STEEL PRODUCTION AND PRICES By Months



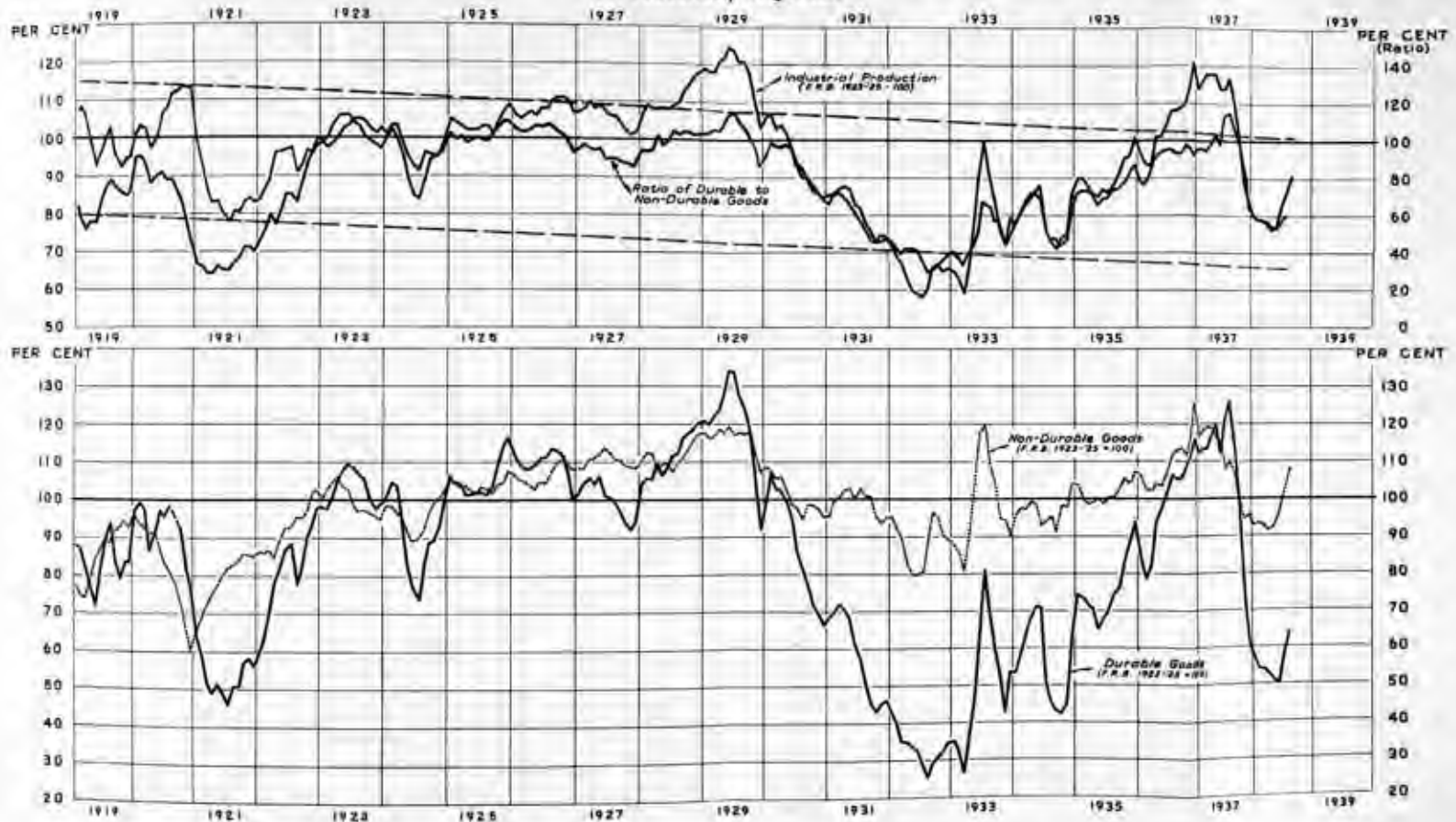
# INDICES OF NEW ORDERS

1936 = 100



# INDUSTRIAL PRODUCTION, AND DURABLE AND NON-DURABLE GOODS PRODUCTION

Seasonally Adjusted



TREASURY DEPARTMENT

38

INTER OFFICE COMMUNICATION

DATE October 17, 1938

TO Secretary Morgenthau

FROM Mr. Haas

Meeting in Mr. Haas' office on October 17, 1938,  
12:05 p.m.

Subject: New Agricultural Program

Present: Jesse W. Tapp, President, Federal Surplus Commodities  
Corporation  
Dr. Thomas Parran, Surgeon General, Bureau of the  
Public Health Service  
Miss Lonigan  
Mr. Haas

Mr. Tapp said that the new agricultural program which has been referred to in the Press as "domestic dumping" of surplus agricultural commodities is not different in nature from what has been going on for some time. The real difference, he pointed out, was that the new program contemplated putting more emphasis on this phase, that is, on subsidizing the consumption of agricultural commodities by low income groups.

He indicated that enlargement of this subsidizing program involved many difficult problems, and at the present time the staff was just in the midst of thinking the matter through.

At the moment consideration was being given to cotton problems. He mentioned the large volume of cotton which is now held under Government loans, and the importance of making some disposition of this cotton. He pointed out further every possible source of outlet in the domestic market was being investigated, and that liquidation of holdings through those outlets would require considerable Government subsidy. He added that one of the main difficulties arose in connection with finished cotton products which were in shape for consumption but in the value of which the cotton formed only a small portion. The program being considered at the present time would cost about \$150 millions, and it would be necessary to go to Congress and ask for an appropriation equal to that amount.

He stated that it was hoped to minimize objections from members of the cotton manufacturing trade, such as the mattress

Secretary Morgenthau - 2 -

manufacturers, by allowing them as well as the relief workers to do some of the processing.

The program as related to other commodities was quite limited in its development at the present time, he stated. The most important problem in connection with the whole arrangement was that of determining the breaking point as between the group of persons who should receive subsidized products and the other group who would have to pay regular prices. He said he was not in favor of setting up what might be called "two parallel economies."

He described an arrangement which existed in New York whereby milk was delivered to certain families at eight cents a quart, and added that a pattern of this sort might be used in some other areas. It might also be applied to some other commodities. But even this arrangement, he stated, was carried out with some difficulty.

He inquired of Dr. Parran if the Public Health officials might not be of some assistance in determining the groups which, because of deficient nutrition, would be entitled to subsidized milk, etc.

Dr. Parran told Mr. Tapp that he would be glad to initiate an experimental survey in an area where he was familiar with the conditions, and that later a pattern so developed might be used in other parts of the country.

Mr. Tapp told Dr. Parran he would get in touch with him later.

Dr. Parran also told Mr. Tapp that he, in cooperation with the Bureau of Home Economics, had worked out a schedule of types of foodstuffs which were now deficient in human diets, and that it had been understood Mr. Tapp's organization was to work out a program of supplying surplus commodities which would fit into this nutritional schedule.

Mr. Tapp explained that this had been done, and that he would be glad to submit a report which would indicate the correlation of surplus commodity distribution with the schedule which Dr. Parran and the Bureau of Home Economics had prepared, and also the progress which had been made to date.



Secretary Morgenthau - 3 -

Mr. Tapp indicated that the distribution program had been expanded beyond what it was assumed would be possible at the time the preliminary program was outlined.

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After the meeting Mr. Tapp told me that Mr. D. W. Bell, Acting Director of the Budget, had told him that the President had approved the plan they had worked out for exchanging wheat for strategic materials, and that it was his understanding that you would not be in the City until Thursday, but in the meantime they were going ahead merely working on the mechanical arrangements which the proposal necessitated.

# The Minneapolis Tribune

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WEDNESDAY, OCTOBER 15, 1914

## 'Dispensing Common Sense.'

It is encouraging to hear a high federal official argue that government should quit calling business names. We must quit "dispensing our common sense in name-calling," was what John W. Hanna, assistant secretary of the treasury, said at the University of Minnesota last week, when he came here to take part in exercises dedicating Vincent Hall, the new home of the School of Business Administration.

Naturally, Mr. Hanna felt that business may have its share of guilt in the name-calling line. Tolerance of various government activities has not always been so generously granted by leaders in the business community. It was, thus, a mutual co-operation which Mr. Hanna described as necessary, but he was more than willing to grant the existence of a mistaken belligerence on the part of government leaders in their dealings with business.

Talk of needed co-operation between elements whose interests center in achievement of identical goals would seem to be a platitude and an unnecessary performance. It ought to be obvious that those who wish to see recovery attained should co-operate in accomplishing that objective. The paradox has persisted, nevertheless. Business, with its tremendous power to give any recovery much needed impetus, has not only been abused under a variety of terms remarkable both for their vagueness and their sustained severity of tone. Business has likewise, during a period of extreme economic difficulty, had to subject itself to staggering tax exactions and to minute and burdensome regulations, seeking to achieve some recovery of a dream.

Mr. Hanna's admissions in his speech here last week are another helpful indication of new ideal changes for the better. The recent denunciation of "Philippine speaker" announcements about friendly relations with business was an affair dignified whose vague promise is now corroborated by the Hanna address. "Co-operation and common sense on the part of government officials and business men," the treasury official said here, "can solve the problems of today and recreate an economically sound America, standing squarely on the principles of free democracy. An economically sound America, putting all its resources to work to meet the needs of all our people, would be an inspiration in a demoralized world."

The nature of his plea for co-operation was clearly indicated by Mr. Hanna when he said: "This plea I make to government officials as well as to the business men of our country." Indication of great importance he attached to a cooperative name of such was his further remark: "The spirit and the will to co-operate is the key to the problems of our national economy today. We must have tolerant cooperation between government and business, and among industry themselves."

Mr. Hanna went a lot farther than the mere suggestion of quieting government in his address at the university. He found himself guilty in which that government would be effective in promoting recovery if both business and government worked together. "Business was not such that where he regarded government as necessary, the business problem was solved, and so were fairly treated, public opinion and the national economy should have been conducted by a congressional committee and the administration."

If the times of responsible government leaders here to Mr. Hanna—being approached as they are expected to be—be far from the effort, with its various various "dispensing and common sense" in Washington, the criticism perhaps because of "dispensing our common sense in name-calling" would be promptly paid, as it should be.

October 17, 1938.

Dear Mr. President:

The events of the past weeks have brought home to all of us the increasing effectiveness of the forces of aggression. Since 1931 we have seen, succeeding each other with briefer and briefer intervals between, the fall of Manchuria and the invasion of China, the conquest of Ethiopia, fomented unrest in Latin America and in the Near East, armed intervention in Spain, the annexation of Austria, and the dismemberment of Czechoslovakia -- All in seven short years.

Nor can we expect aggression to end there. Japan at first wanted only Manchuria; then North China; now she will not be content with less than the whole of China. Italy wanted only Ethiopia; now she wants control of North Africa. Germany wanted only equality in armaments, then the remilitarization of the Rhineland, then Austria, then Czechoslovakia, now colonies. The current claim of an aggressor power is always its last -- until the next one.

So well have the aggressor nations mastered the tactics of aggression that a victory in one part of the world is followed by outbursts of aggression elsewhere. Germany's victory in Czechoslovakia is followed with indecent haste by Polish and Hungarian demands. Japan, watching her opportunity, loses no time in attacking Canton, while in Palestine, Arab discontent is fomented to fever pitch.

We should learn the lesson which the history of the last seven years has to teach us. Let us not repeat the short-sighted mistakes of Britain and France. The impact of the aggressor nations upon American life and American interests has so far, to be sure, been more insidious than overt but it will be too late if we wait until the effects are obvious. Who in France as late as 1920 would have dreamt that in less than a decade that great democratic nation was to become a second-rate power, shorn of influence in central Europe, dependent upon a grudging and demanding ally for security? Who would have expected that Great Britain's might would be challenged in the Mediterranean, that her economic interests would be brushed aside in China, and that the Premier of England would hurry to Hitler to plead that he be not too demanding or impatient, and to plead, moreover in humble tones lest the dictator take umbrage and demand more?

- 2 -

Let us while we can peacefully do so try to check the aggressors. Let us not be placed in the position of having to compound with them. Let it not be necessary for the President of the United States to fly to Tokyo and in humble manner plead with the Mikado that he be content with half the Philippines rather than wage war for the whole. Such a possibility may seem ridiculous now, but no more ridiculous than Chamberlain's flight to Berlin would have seemed seven years ago.

In March of this year Winston Churchill called upon England to act, saying "If we do not stand up to the dictators now, we shall only prepare the day when we shall have to stand up to them under far more adverse conditions. Two years ago it was safe, three years ago it was easy, and four years ago a mere dispatch might have rectified the position... Now the victors are the vanquished, and those who threw down their arms in the field and sued for an armistice are striding on to world mastery." The basis for the present humiliation of England was laid in 1931, when England failed to join the United States in disapproval of Japanese aggression in Manchuria. The basis of either humiliation or war for the United States is being laid today by a foreign policy that shuts its eyes to aggression and withholds economic support from those who resist.

I know you are firmly convinced as I am firmly convinced that the forces of aggression must be stopped. By whom if not by us? I believe that we are the only country in the world now in a position to initiate effective steps to stop aggression by peaceful means. Once the United States takes the lead in developing an effective program, democratic forces in all countries -- even those now submerged in the aggressor nations -- will take heart. In England and in France groups within the government and without will be stimulated and encouraged to press for parallel action.

To use our great financial strength to help safeguard future peace for the United States, and to make your "Good Neighbor" policy really effective, we should introduce at once a program of peaceful action on two fronts -- in the Far East and in Latin America. In these two areas we can move most effectively and with the least complication.

Two opportunities are now before us:

1. The extension of credit to China. It is yet possible for such aid to be of decisive help. Sanguine as I desire to be, I am forced to the view that without substantial financial aid given promptly the Chinese resistance may soon disintegrate. By risking little more than the cost of one battleship we can give renewed vitality and effectiveness to the Chinese. We can do more than that. By our action we can further the struggle of democracy against aggression everywhere.

I am pleading China's cause with a special urgency because you have on numerous occasions told me to proceed with proposals for assistance to China. All my efforts to secure immediate substantial aid for China have proved of no avail against the adamant foreign policy of doing nothing which could possibly be objected to by an aggressor nation. I need not tell you that I respect the integrity and sincerity of those who hold the belief that a course of inaction is the right one, but the issues at stake go beyond any one of us and do not permit me to remain silent. What greater force for peace could there be than the emergence of a unified China?

2. The extension of credit to Latin American countries.

Our neighbors to the south are sorely in need of capital and commerce to enable them to develop their resources free from foreign intervention. Unless we assist them they will become a helpless field for political and economic exploitation by the aggressor nations. Already some inroads have been made in that direction. Now, after the Munich agreement, we may expect that Germany, Italy and Japan will become bolder and more effective in their attempts to establish areas of economic and political support to the south of us. We can stop that penetration by an intelligent use of a small proportion of our enormous gold and silver holdings.

The measures we may adopt can be developed as the specific occasions requiring assistance may arise. We have several such occasions before us right now: Brazil, Cuba, Mexico, Peru. The details of the assistance can be worked out in conjunction with the representatives of those governments, but it is first necessary that we accept in principle the need for positive action of this kind as a part of our "Good Neighbor" policy.

European events of the last month have made me feel more certain than ever of the wisdom of initiating a positive program of assistance along the lines indicated above. Reports from China convince me that the need for quick action is urgent.

Sincerely,

The President,  
Hyde Park, N. Y.

Copy

October 17, 1938.

Dear Mr. President:

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We should learn the lesson which the history of the last seven years has to teach us. Let us not repeat the short-sighted mistakes of Britain and France. The impact of the aggressor nations upon American life and American interests has so far, to be sure, been more insidious than overt but it will be too late if we wait until the effects are obvious. Who in France as late as 1930 would have dreamt that in less than a decade that great democratic nation was to become a second-rate power, shorn of influence in central Europe, dependent upon a grudging and demanding ally for security? Who would have expected that Great Britain's might would be challenged in the Mediterranean, that her economic interests would be brushed aside in China, and that the Premier of England would hurry to Hitler to plead that he be not too demanding or impatient, and to plead, moreover in humble tones lest the dictator take umbrage and demand more?

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Sincerely,

The President,  
Hyde Park, N. Y.



Dear Mr. President:

I have found myself in the last few days continually reviewing the past weeks of tension. I am greatly troubled, Mr. President. I have been troubled for a long time. I feel that in the light of the dominant forces which are shaping the world's course we must re-examine our foreign policy.

The events of the past weeks have ~~with shock~~ brought home ~~to us~~ to all of us the increasing <sup>efficiency</sup> ~~aggressiveness~~ of the forces of aggression. Since 1931 we have seen, succeeding each other with briefer and briefer intervals between, the fall of Manchuria and the military invasion of China, the conquest of Ethiopia, fomented unrest in Latin America and in the Near East, armed intervention in Spain, the annexation of Austria, and the dismemberment of Czechoslovakia.

All this ~~has happened~~ in seven <sup>short</sup> years.

Seven years are not long even in our own lives. In the life of a nation they are terrifyingly short. Is there any reason, ~~Mr. President,~~ to expect that ~~aggression will end~~ there?

*How can we expect to aggress to end this*

Japan at first wanted only Manchuria; then North China; now she will not be content with less than the whole of China. Italy wanted only Ethiopia; now she wants control of Spain

*W. C. C. C.*

10/15/38

*There is no other*

- 2 -

and North Africa. Germany wanted only equality in armaments, then the remilitarization of the Rhineland, then Austria, then Czechoslovakia, now colonies. The current claim of an aggressor power is always its last -- until the next one.

~~Each conquest is but the prelude to the next.~~ So well have the aggressor nations mastered the tactics of aggression that a victory in one part of the world is followed by outbursts of aggression elsewhere. ~~Thus steps which appear isolated and born of the moment emerge in reality as a coherent pattern of successive victories for aggression.~~ Hitler's victory in Czechoslovakia is followed with indecent haste by Polish and Hungarian demands. Japan, watching her opportunity, loses no time in attacking Canton, while in Palestine, Arab discontent is fomented to fever pitch.

What expectation may we have save more aggression -- each stroke bolder than the last, each wave of diplomatic and military conquest involving wider areas? Time and again it has been proved that no reliance can be placed on the pacific utterances of the aggressor powers. Japan's objective is not less than the domination of Eastern Asia. Germany will not rest until she has no rivals in Europe. Italy means to dominate the Mediterranean basin.

We cannot lull ourselves into believing that the trend of events in Europe and in Asia will not affect us. Already it has begun to impinge upon every aspect of our national life.

*Should*

- 3 -

out

Our international trade is being forced into ever-narrowing channels. More and more areas of trade are being dominated by clearing agreements, barter practices, blocked balances, multiple currencies, and other devices which run counter to the trade policy the United States has been pursuing. And as the area of domination increases, third countries will be driven to adopt trade practices which will still further reduce the markets in which our exporters can freely trade.

The changes which take place in the wake of aggression may thus far more than offset the gains achieved through our trade agreements program. I do not mean to imply that our trade agreements program has not achieved results. I merely wish to point out that these results are being vitiated by the policy of aggressor nations and that the continuation of the present trend may well see a complete disruption of the program.

Only in the last week J. M. Keynes recommended that the British Government pursue a policy directed toward closer approach to bilateral balancing of trade. If Great Britain establishes such a precedent, it is difficult to see how any country can refrain from following, and the end result for us would be a complete rout of our commercial policy.

Aggression impinges on our monetary policy too. Japan's invasion of China forces her to sell all her silver to us.

- 4 -

This induces other countries to give up the metal as a monetary stock, with obvious repercussions on the value of our own silver assets. Even the important role played by gold is being seriously interfered with. Continued world tensions intensify maldistribution of the world's gold and make subsequent redistribution yet more difficult. It is not at all certain that we shall ever be able to get rid of our enormous surplus of gold and silver. But more disquieting than all this is the prospect of increasing weakness in European currencies. Eventually both England and France may be driven to adopt practices which not only will disrupt the Tripartite Accord but will set the stage for the complete breakdown of international monetary relationships as we now know them. Frankly, Mr. President, I am disturbed by the possibilities that lie ahead of us in the monetary field.

Nor can I regard without concern the additional tax burdens arising from the increased tempo of the world armaments race. America cannot hope to escape joining in that race. In a world in which international anarchy is but a step removed it would be suicidal, I know you feel and I feel, not to maintain adequate military power to defend ourselves against aggression. The stronger the aggressor powers grow, the greater will be our need for armaments. It is probably not an understatement to say that Germany's recent diplomatic victory in Czechoslovakia will cost the people of the United States billions of dollars in war preparedness.

- 5 -

And if Japan succeeds in taking over China, the sum will have to be doubled at least.

But all these economic losses, great though they are, are of secondary importance. The noxious effects of victorious aggression impinge alarmingly on our social, political, and cultural life. With every stride forward of the aggressor nations, political security in the United States recedes, political tensions increase, antagonisms between various minority racial and religious groups are sharpened. Already on this side of the Atlantic there have arisen a score of insidious growths, innocent looking enough, but bearing within the germs of the same poisons that have well nigh destroyed civilization in half of Europe.

*We should*  
 Mr. President, let us learn well the lesson which the history of the last seven years has to teach us. Let us not repeat the *short-sighted* ~~myopic~~ mistakes of Britain and France. The impact of the aggressor nations upon American life and American interests is *so far* more insidious than overt. But we ~~cannot afford to wait~~ until the effects are spectacular. *it will be too late if we*  
 Who in France as late as 1930 could have dreamt that in less than a decade that great democratic nation was to become a second-rate power, shorn of influence in central Europe, dependent upon a grudging and demanding ally for security? Who would have expected that Great Britain's might would be challenged in the Mediterranean, that her economic interests

- 6 -

would be brushed aside in China, and that the Premier of England would hurry to Hitler to plead that he be not too demanding or impatient, and to plead, moreover in humble tones lest the dictator take umbrage and demand more?

~~Mr. President, let us not join in the retreat of Great Britain and France.~~ Let us while we can peacefully do so stop the aggression which it is yet in our power to stop. Let us not be placed in the position of having to compound with the aggressor. Let it not be necessary for the President of the United States to fly to Tokyo and in humble manner plead with the Mikado that he be content with half the Philippines rather than wage war for the whole. Such a possibility may seem ridiculous now, but no more ridiculous than Chamberlain's flight to Berlin would have seemed seven years ago.

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- 7 -

United States in disapproval of Japanese aggression in Manchuria. The basis of either humiliation or war for the United States is being laid today by a foreign policy that shuts its eyes to aggression and withholds moral and economic support from those who resist.

The weakness of democratic countries has lain as much in their passivity to a process of attrition as in their resigned acceptance of the violent fait accompli. Whether knowingly or not, they have helped the aggressor to power by facilitating a gradual and insidious process of economic and political penetration. They have done this by extending credits, by making trade agreements, by relaxing previous commercial and financial agreements and claims, by leaving the field wide open in third countries to the use of those economic practices which lead to the domination of the aggressor nations. This policy is being carried out on the theory that the belligerence of the aggressor powers can be lessened by peaceful concessions. Actually concessions only increase their power and therefore their belligerence. Experience has shown that you cannot tame the tiger by throwing crumbs to him. In every concession to their demands the aggressor nations, convinced of the decadence of democracy, see only a sign of weakness, of resignation, and of abdication.

This path must not be trodden by the United States. We must not compound with the aggressors by arranging first a

- 3 -

little financial credit, then a commercial understanding, then a trade agreement; one concession following another until we suddenly realize that we have made more powerful the very nations which ultimately threaten everything the United States stands for.

At this very moment there are powerful influences in and out of our government which are already seeking to lure us to this path. We shall no doubt be soon invited -- directly or indirectly -- by the British and French Governments to help foot the bill of their folly; we shall be called upon to smooth the road of the aggressor nations toward an (illusory satiety.) Contradictory arguments will be used to inveigle us. It will be claimed on the one hand that financial and commercial agreements will be part of the universal process of "appeasement". On the other hand it will be urged that we should not allow moral and political considerations to influence our commercial and economic policy, and that such agreements will promote trade and contribute to American prosperity. Mr. President, the dangers of yielding to the blandishments of "commerce" are the greater because they are more subtle.

As I review our foreign policy of the last few years, I note how step by step we have followed the ineffectual, misdirected policy of the present British Government. Mr. President, we must break the mis-leading strings of Great Britain. We must assume leadership ourselves and then

2b- 10/15/38



~~Who's responsible~~  
~~to act to make~~  
~~peace~~

England will follow. I know you are firmly convinced as I am firmly convinced that the forces of aggression must be stopped. By whom if not by us? I believe that we are the only country in the world now in a position to initiate effective steps to stop aggression by peaceful means. Once the United States takes the lead in developing an effective program, democratic forces in all countries -- even those now submerged in the aggressor nations -- will take heart. In England and in France groups within the government and without will be stimulated and encouraged to press for parallel action.

By initiative I do not have in mind the issuance of another State document, however determined in tone. The reiteration of policy unsupported by corresponding action serves ultimately only to arouse derision abroad and to confuse public opinion at home. The trade agreements program which we have been pursuing has indeed been a program of action, but I trust you will not think me ungenerous when I say that its potency against the forces of aggression is slight.

~~We cannot wait to take other positive and more effective steps, Mr. President.~~ <sup>We must</sup> introduce at once a program of peaceful action on two fronts -- in the Far East and in Latin America. In these two areas we can move most effectively and with the least complication.

2b- 10/15/38

To use our great international financial strength to help safeguard future peace for the U.S., and to make your "Good Neighbor" policy really work.

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Two opportunities are now before us:

1. The extension of credit to China. It is yet possible for such aid to be of decisive help. Sanguine as I desire to be, I am forced to the view that without substantial financial aid the Chinese resistance may quickly disintegrate. By risking little more than the cost of one battleship we can give renewed vitality to Chinese morale and effectiveness. We can do more than that. By our action we can further the struggle of democracy against aggression everywhere.

~~Mr. President,~~ I am taking the liberty of pleading China's cause with a special urgency because you have <sup>on numerous</sup> ~~three~~ <sup>occasions</sup> ~~told me~~ to proceed with proposals for assistance to China. All my efforts to secure immediate substantial aid for China have proved of no avail against the adamant foreign policy of doing nothing which could possibly be objected to by an aggressor nation. I need not tell you that I respect the integrity and sincerity of those who hold the belief that a course of inaction is the right one, but the issues at stake go beyond any one of us and do not permit me to remain silent. What greater force for peace could there be, ~~Mr. President,~~ than the emergence of a unified ~~and victorious~~ China?

2. The extension of credit to Latin American countries. Our neighbors to the south are sorely in need of capital and commerce to enable them to develop their resources free

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from foreign intervention. Unless we assist them they will become a helpless field for political and economic exploitation by the aggressor nations. Already some inroads have been made in that direction. Now, after the Munich agreement, we may expect that Germany, Italy and Japan will become bolder and more effective in their attempts to establish <sup>real</sup> islands of economic and political support to the south of us. We can stop that penetration by an intelligent use of a <sup>small</sup> ~~small~~ negligible proportion of our enormous gold and silver holdings.

The measures we may adopt can be developed as the specific occasions requiring assistance may arise. We have several such occasions before us right now: Brazil, Cuba, Mexico, Peru. The details of the assistance can be worked out in conjunction with the representatives of those governments, but it is first necessary that we accept in principle the need for positive action of this kind as a part of our foreign policy.

~~Mr. President, I beg that you will not let pass this historic opportunity for initiating effective economic measures against aggression, measures which at the same time will be moral gestures sorely needed in a world in which "appeasement" has superseded morality. I have never felt more profoundly the need for such action. I have never felt more certain of its wisdom.~~

HDW:HG:SA:lrs  
2b- 10/15/38



THE SECRETARY OF THE TREASURY  
WASHINGTON

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ZAK

Dear Mr. President:

I have found myself in the last few days continually reviewing the past weeks of tension. I am greatly troubled, Mr. President. I have been troubled for a long time. I feel that in the light of the dominant forces which are shaping the world's course we must re-examine our foreign policy.

The events of the past weeks have with a shock brought home to ~~me~~ all of us the increasing explosiveness of the forces of aggression. Since 1931 we have seen, succeeding each other with briefer and briefer intervals between, the fall of Manchuria and the ~~military~~ invasion of China, the conquest of Ethiopia, fomented unrest in Latin America and in the Near East, armed intervention in Spain, the annexation of Austria, and the dismemberment of Czechoslovakia.

All this has happened in seven <sup>short</sup> years.

Seven years are not long even in our own lives. In the life of a nation they are terrifyingly short. Is there any reason, Mr. President, to expect that aggression will end there?

Japan at first wanted only Manchuria; then North China; now she will not be content with less than the whole of China. Italy wanted only Ethiopia; now she wants control of Spain

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and North Africa. Germany wanted only equality in armaments, then the remilitarization of the Rhineland, then Austria, then Czechoslovakia, now colonies. The current claim of an aggressor power is always its last -- until the next one.

~~Each conquest is but the prelude to the next.~~ So well have the aggressor nations mastered the tactics of aggression that a victory in one part of the world is followed by outbursts of aggression elsewhere. ~~(Thus steps which appear isolated and born of the moment emerge in reality as a coherent pattern of successive victories for aggression.)~~ Hitler's victory in Czechoslovakia is followed with indecent haste by Polish and Hungarian demands. Japan, watching her opportunity, loses no time in attacking Canton, while in Palestine, Arab discontent is fomented to fever pitch.

What expectation may we have save more aggression-- each stroke bolder than the last, each wave of diplomatic and military conquest involving wider areas? Time and again it has been proved that no reliance can be placed on the pacific utterances of the aggressor powers. Japan's objective is not less than the domination of Eastern Asia. Germany will not rest until she has no rivals in Europe. Italy means to dominate the Mediterranean basin.

We ~~cannot~~ <sup>should not</sup> lull ourselves into believing that the trend of events in Europe and in Asia will not affect us. Already it has begun to impinge upon every aspect of our national life.

- 3 out

Our international trade is being forced into evernarrowing channels. More and more areas of trade are being dominated by clearing agreements, barter practices, blocked balances, multiple currencies, and other devices which run counter to the trade policy the United States has been pursuing. And as the area of domination increases, third countries will be driven to adopt trade practices which will still further reduce the markets in which our exporters can freely trade.

The changes which take place in the wake of aggression may thus far more than offset the gains achieved through our trade agreements program. I do not mean to imply that our trade agreements program has not achieved results. I merely wish to point out that these results are being vitiated by the policy of aggressor nations and that the continuation of the present trend may well see a complete disruption of the program.

Only in the last week J. M. Keynes recommended that the British Government pursue a policy directed toward closer approach to bilateral balancing of trade. If Great Britain establishes such a precedent, it is difficult to see how any country can refrain from following, and the end result for us would be a complete rout of our commercial policy.

Aggression impinges on our monetary policy too. Japan's invasion of China forces her to sell all her silver to us.

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out

This induces other countries to give up the metal as a monetary stock, with obvious repercussions on the value of our own silver assets. Even the important role played by gold is being seriously interfered with. Continued world tensions intensify maldistribution of the world's gold and make subsequent redistribution yet more difficult. It is not at all certain that we shall ever be able to get rid of our enormous surplus of gold and silver. But more disquieting than all this is the prospect of increasing weakness in European currencies. Eventually both England and France may be driven to adopt practices which not only will disrupt the Tripartite Accord but will set the stage for the complete breakdown of international monetary relationships as we now know them. Frankly, Mr. President, I am disturbed by the possibilities that lie ahead of us in the monetary field.

Nor can I regard without concern the additional tax burdens arising from the increased tempo of the world armaments race. America cannot hope to escape joining in that race. In a world in which international anarchy is but a step removed it would be suicidal, I know you feel and I feel, not to maintain adequate military power to defend ourselves against aggression. The stronger the aggressor powers grow, the greater will be our need for armaments. It is probably not an understatement to say that Germany's recent diplomatic victory in Czechoslovakia will cost the people of the United States billions of dollars in war preparedness.

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And if Japan succeeds in taking over China, the sum will have to be doubled at least.

But all these economic losses, great though they are, are of secondary importance. The noxious effects of victorious aggression impinge alarmingly on our social, political, and cultural life. With every stride forward of the aggressor nations, political security in the United States recedes, political tensions increase, antagonisms between various minority racial and religious groups are sharpened. Already on this side of the Atlantic there have arisen a score of insidious growths, innocent looking enough, but bearing within the germs of the same poisons that have well nigh destroyed civilization in half of Europe.

~~Mr. President, let us~~ <sup>we should</sup> learn well the lesson which the history of the last seven years has to teach us. Let us not repeat the <sup>short sighted</sup> ~~myopic~~ mistakes of Britain and France. The impact of the aggressor nations upon American life and American interests is <sup>so far</sup> more insidious than overt. But we cannot afford to wait until the effects are spectacular. Who in France as late as 1930 could have dreamt that in less than a decade that great democratic nation was to become a second-rate power, shorn of influence in central Europe, dependent upon a grudging and demanding ally for security? Who would have expected that Great Britain's might would be challenged in the Mediterranean, that her economic interests



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would be brushed aside in China, and that the Premier of England would hurry to Hitler to plead that he be not too demanding or impatient, and to plead, moreover in humble tones lest the dictator take umbrage and demand more?

~~Mr. President, let us not join in the retreat of Great Britain and France.~~ Let us while we can peacefully do so stop the aggression which it is yet in our power to stop. Let us not be placed in the position of having to compound with the aggressor. Let it not be necessary for the President of the United States to fly to Tokyo and in humble manner plead with the Mikado that he be content with half the Philippines rather than wage war for the whole. Such a possibility may seem ridiculous now, but no more ridiculous than Chamberlain's flight to Berlin would have seemed seven years ago.

In March of this year Winston Churchill called upon England to act, saying "If we do not stand up to the dictators now, we shall only prepare the day when we shall have to stand up to them under far more adverse conditions. Two years ago it was safe, three years ago it was easy, and four years ago a mere dispatch might have rectified the position ... Now the victors are the vanquished, and those who threw down their arms in the field and sued for an armistice are striding on to world mastery." The basis for the present humiliation of England was laid in 1931, when England failed to join the

See [unclear]  
[unclear]

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United States in disapproval of Japanese aggression in Manchuria. The basis of either humiliation or war for the United States is being laid today by a foreign policy that shuts its eyes to aggression and withholds moral and economic support from those who resist. A

The weakness of democratic countries has lain as much in their passivity to a process of attrition as in their resigned acceptance of the violent fait accompli. Whether knowingly or not, they have helped the aggressor to power by facilitating a gradual and insidious process of economic and political penetration. They have done this by extending credits, by making trade agreements, by relaxing previous commercial and financial agreements and claims, by leaving the field wide open in third countries to the use of those economic practices which lead to the domination of the aggressor nations. This policy is being carried out on the theory that the belligerence of the aggressor powers can be lessened by peaceful concessions. Actually concessions only increase their power and therefore their belligerence. Experience has shown that you cannot tame the tiger by throwing crumbs to him. In every concession to their demands the aggressor nations, convinced of the decadence of democracy, see only a sign of weakness, of resignation, and of abdication.

This path must not be trodden by the United States. We must not compound with the aggressors by arranging first a

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little financial credit, then a commercial understanding, then a trade agreement; one concession following another until we suddenly realize that we have made more powerful the very nations which ultimately threaten everything the United States stands for.

At this very moment there are powerful influences in and out of our government which are already seeking to lure us to this path. We shall no doubt be soon invited -- directly or indirectly -- by the British and French Governments to help foot the bill of their folly; we shall be called upon to smooth the road of the aggressor nations toward an illusory satiety. Contradictory arguments will be used to inveigle us. It will be claimed on the one hand that financial and commercial agreements will be part of the universal process of "appeasement". On the other hand it will be urged that we should not allow moral and political considerations to influence our commercial and economic policy, and that such agreements will promote trade and contribute to American prosperity. Mr. President, the dangers of yielding to the blandishments of "commerce" are the greater because they are more subtle.

As I review our foreign policy of the last few years, I note how step by step we have followed the ineffectual, misdirected policy of the present British Government. Mr. President, we must break the mis-leading strings of Great Britain. We must assume leadership ourselves and then

A. M.

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England will follow. I know you are firmly convinced as I am firmly convinced that the forces of aggression must be stopped. By whom if not by us? I believe that we are the only country in the world now in a position to initiate effective steps to stop aggression by peaceful means. Once the United States takes the lead in developing an effective program, democratic forces in all countries -- even those now submerged in the aggressor nations -- will take heart. In England and in France groups within the government and without will be stimulated and encouraged to press for parallel action.

~~By initiative I do not have in mind the issuance of another State document, however determined in tone. The reiteration of policy unsupported by corresponding action serves ultimately only to arouse derision abroad and to confuse public opinion at home. The trade agreements program which we have been pursuing has indeed been a program of action, but I trust you will not think me ungenerous when I say that its potency against the forces of aggression is slight.~~

~~We cannot wait to take other positive and more effective steps, Mr. President.~~ We must introduce at once a program of peaceful action on two fronts -- in the Far East and in Latin America. In these two areas we can move most effectively and with the least complication.

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Two opportunities are now before us:

1. The extension of credit to China. It is yet possible for such aid to be of decisive help. Sanguine as I desire to be, I am forced to the view that without substantial financial aid the Chinese resistance may quickly disintegrate. By risking little more than the cost of one battleship we can give renewed vitality to Chinese morale and effectiveness. We can do more than that. By our action we can further the struggle of democracy against aggression everywhere.

~~Mr. President,~~ I am taking the liberty of pleading China's cause with a special urgency because you have <sup>numerous occasions</sup> ~~three~~ times told me to proceed with proposals for assistance to China. All my efforts to secure immediate substantial aid for China have proved of no avail against the adamant foreign policy of doing nothing which could possibly be objected to by an aggressor nation. I need not tell you that I respect the integrity and sincerity of those who hold the belief that a course of inaction is the right one, but the issues at stake go beyond any one of us and do not permit me to remain silent. What greater force for peace could there be, ~~Mr. President,~~ than the emergence of a unified ~~and independent~~ China?

2. The extension of credit to Latin American countries. Our neighbors to the south are sorely in need of capital and commerce to enable them to develop their resources free

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from foreign intervention. Unless we assist them they will become a helpless field for political and economic exploitation by the aggressor nations. Already some inroads have been made in that direction. Now, after the Munich agreement, we may expect that Germany, Italy and Japan will become bolder and more effective in their attempts to establish ~~islands~~ <sup>areas</sup> of economic and political support to the south of us. We can stop that penetration by an intelligent use of a *small* ~~negligible~~ proportion of our enormous gold and silver holdings.

The measures we may adopt can be developed as the specific occasions requiring assistance may arise. We have several such occasions before us right now: Brazil, Cuba, Mexico, Peru. The details of the assistance can be worked out in conjunction with the representatives of those governments, but it is first necessary that we accept in principle the need for positive action of this kind as a part of our foreign policy.

Mr. President, I beg that you will not let pass this historic opportunity for initiating effective economic measures against aggression, measures which at the same time will be moral gestures sorely needed in a world in which "appeasement" has superseded morality. I have never felt more profoundly the need for such action. I have never felt more certain of its wisdom.

(First Draft)

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Dear Mr. President:

I have found myself in the last few days continuously reviewing the past weeks of tension. I am greatly troubled, Mr. President. I have been troubled for a long time. I feel that now I must speak out.

The events of the past weeks have with a shock brought home to me as to all of us the increasing explosiveness of the forces of aggression. Since 1931 we have seen, succeeding each other with briefer and briefer intervals between, the fall of Manchuria and the military invasion of China, the conquest of Ethiopia, armed intervention in Spain, the annexation of Austria, the dismemberment of Czechoslovakia and fomented unrest in the Near East and in Latin America.

All this has happened in seven years.

Seven years are not long even in our own lives. In the life of a nation they are terrifyingly short. Is

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there any reason, Mr. President, to expect that aggression will end there? Is there any reason to expect that the explosiveness of the aggressor powers will not be redoubled in the next seven years? These forces will not stop of their own momentum. The appetite grows on what it feeds upon. "Fascism's demand" -- I quote Thomas Mann -- "cannot be satisfied and quieted with concessions, but are thoroughly vague, indefinable, and boundless." Japan at first wanted only Manchuria; then North China; now she will not be content with less than the whole of China. Italy wanted only Ethiopia; now she wants control of Spain and North Africa. Germany wanted only equality in armaments, then the Saar, then Austria, then Czechoslovakia, now colonies. The current claim of an aggressor power is always its last -- until the next one. After China, the Asiatic mainland; after Spain, the Mediterranean basin; after Czechoslovakia, the Balkans, colonies, the Ukraine.



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Before it conquered Manchuria the Japanese Government time and again publicly announced that it had no territorial designs on Manchuria. It said the same thing about North China before it entered North China, and repeated it for China as a whole before it entered the Yangtze Valley. On the other hand, innumerable unofficial and semi-official statements exist making clear that Japan's objective is not less than the domination of Eastern Asia.

Similarly with Germany. Before it remilitarized the Rhineland it officially announced that it stood by the Locarno Pact. Before it took over Austria it had publicly recognized its independence. Before it dismembered Czechoslovakia Germany had announced it had no territorial designs on Czechoslovakia. Now Hitler says he has no further territorial designs in Europe. Yet a reading of Mein Kampf will demonstrate clearly that the steps he has

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taken up to now are all part of a wider program which involves further aggression and further expansion of Germany's area of control.

And so too, Italy has proclaimed time and again that her intentions in Ethiopia were peaceful. Mussolini after his military victory in Ethiopia announced that Italy could henceforth be recognized among the "satisfied powers", yet within a few months we find Italy involved in Spain and North Africa, seeking to increase by force her sphere of influence. (If, Mr. Secretary, you feel that this point should be developed, we have detailed quotations, etc.)

Is there anything that can stop the aggressors? You and I had hoped that the democratic powers of Europe and their allies would erect barriers to aggressive expansion. Recent events compel us drastically to revise this expec-

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tation. France is no longer a first rate power. England has resigned herself to a policy of further concessions to the aggressor. Democracy in Europe seems to have surrendered before the onslaught.

We cannot lull ourselves into believing that the trend of events in Europe and in Asia will not affect us. What has taken place in Europe and in Asia has already begun to impinge upon every aspect of our national life.

Our international trade is being forced into ever-narrowing channels. More and more areas of trade are being dominated by clearing agreements, barter practices, blocked balances, multiple currencies, and other devices which run counter to the trade policy the United States has been pursuing.

The sphere of our trade agreements is contracting as the area of political and economic domination

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of Germany and Japan expands. We have seen what Japan has done with our trade in Manchuria and what she is doing with our trade in North China and the Yangtze Valley. We have seen that gainful trade agreements with Chile, Turkey, Greece (and Peru?) have not yet been possible because of practices imposed by Germany on trade with those countries. The value of existing trade agreements has been diminished by Germany's trade tactics. Our agreement with Czechoslovakia is now of little value. Our agreement with Brazil has worked badly. The possibility of future gainful trade agreements with the countries of central and southeastern Europe -- Poland, Rumania, Bulgaria, Jugoslavia, Hungary, Greece and Turkey -- has now become negligible.

Likewise our trade with third countries suffers. The expansion of the aggressor nations strikes at our trade with countries who buy from us. Germany's resort

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to clearing agreements and barter devices is cutting heavily into Britain's exports in Latin America and elsewhere. England sells less and is therefore able to buy less and so we find our business with third countries less than it otherwise would be. Furthermore, third countries are driven to adopt trade practices which still further will reduce the area in which our exporters can freely operate. The behaviour of the aggressor nations may far more than offset the gains to our trade resulting from our trade agreements program. I do not mean to imply that our trade agreements program has not achieved results. I merely wish to point out that these results are being vitiated by the policy of aggressor nations and that the continuation of the present trend may well see a complete disruption of the program.

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In the field of international monetary affairs likewise aggression has brought trouble. The weakness of the European currencies is enhanced by Germany's economic and political tactics. The value of the Tripartite Accord will be greatly impaired in the event of another serious decline in the franc. ~~It is even doubtful whether the Accord could survive such a decline.~~ Nothing is calculated more to weaken the franc than the growing power of Germany. British opinion appears to be already crystallizing in favor of a lower sterling rate. Any further substantial depreciation of foreign currencies may serve to wipe out the gains from the concessions we have obtained in numerous trade agreements.

Japan's invasion of China has caused China to abandon silver as a medium of exchange and thereby increased the incentive of other countries to give up silver in their

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monetary stock, with obvious repercussions on our own silver policy. On the other hand, continued world tensions are tending to cause the concentration of the world's gold in the United States. Should war break out, it is quite possible that we would get so much of the world's gold as to make impossible any subsequent redistribution of the world's gold holdings.

But our loss in trade is only a part, and a small part, of the losses we will sustain as a consequence of the present trend in world events. The armament race which, despite well-wishes to the contrary, will go on at an increasing tempo, and to the ordinary expenditures of armies and navies will be added the costly burden of preparing defenses against air raids. American cannot hope to escape the need for joining in this race. In a

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world in which international anarchy is but a step removed it would be suicidal, I know you feel and I feel, not to maintain adequate military power to defend ourselves against aggressions. The stronger the aggression powers grow, the greater will be our need for armaments. It is probably not an understatement to say that Hitler's recent diplomatic victory in Czechoslovakia will cost the people of the United States hundreds of millions in war preparedness. Of the cost of our involvement in war I will not speak. But can we say that such an involvement is impossible or even unlikely if the aggressor powers continue to expand?

But all these economic losses, great though they are, are of secondary importance. Far more destructive are the effects on our social, political, and cultural life. With every stride forward of the aggressor nations, political



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security in the United States recedes, political tensions increase, antagonisms between various minority racial and religious groups are sharpened. Foreign propaganda daily becomes more rampant, and the free exercise of our civil liberties more difficult. I am deeply concerned about the influence of the effects on our own democracy of the retreat of democracies abroad.

With ever increasing revulsion you and I have watched the long tradition of culture and civilization, so painfully acquired throughout thousands of years, being swept brutally and boastfully away, and in their place intolerance, cruelty, persecution, and spiritual degradation being enthroned. The bully's threat, oppressive power, becomes the arbiter of nations. Strong nations are made weak and weak nations crushed. The rules of gangsterdom become

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the laws of civilization. International anarchy looms.

Mr. President, let us learn well the lesson which the history of the last seven years has to teach us. Let us not repeat the myopic mistakes of Britain and France. The impact of the aggressor nations upon American life and American interests is more insidious than overt. But we cannot afford to wait until the effects are spectacular. Who in France as late as 1930 could have dreamed that in less than a decade that great democratic nation was to become a second-rate power, short of influence in central Europe, dependent upon a grudging and demanding

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ally for security, and condemned the world over by people who regard as sacred a nation's given word? Who would have expected that Great Britain's might would be challenged in the Mediterranean, that its economic interests would be lightly brushed aside in China, and that the Premier of England would hurry to Hitler to plead that he be not too demanding or impatient, and to plead, moreover in humble tones lest the dictator take umbrage and demand more? Who would have suspected a small nation could disappear from the map overnight, that the horrors of Nanking and Guernica could be perpetrated, much less that their perpetration would awaken neither official censure nor meaningful public condemnation; who would have thought that defenseless civilians in Nanking, Canton, Barcelona, and a hundred other places could be repeatedly and mercilessly bombed with no more than feeble protest

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by the civilized nations; or that a single government could threaten to plunge the whole world into war if it didn't get what it wanted, when it wanted it? Yet these things have come to pass and many more such will come to pass, I fear, while the possibility of stopping them by peaceful means grows less and less. In March of this year Winston Churchill called upon England to act, saying "If we do not stand up to the dictators now, we shall only <sup>delay</sup> prepare the day when we shall have to stand up to them under far more adverse conditions. Two years ago it was safe, three years ago it was easy, and four years ago a mere dispatch might have rectified the position ... Now the victors are the vanquished, and those who threw down their arms in the field and sued for an armistice are striding on to world mastery."

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Mr. President, let us not join in the retreat of Great Britain and France. Let us while we can peacefully do so stop the aggression which it is yet in our power to stop. Let us not be placed in the position of having to compound with the aggressor. Let it not be necessary for the President of the United States to fly to Tokyo and in humble manner plead with the Mikado that he be content with half the Philippines rather than wage war for the whole. Such a possibility may seem ridiculous now, but no more ridiculous than Chamberlain's flight to Berlin would have seemed seven years ago. The basis for the present humiliation of England was laid in 1931, when England failed to join the United States in disapproval of Japanese aggression in Manchuria. The basis of the humiliation of the United States of America is being laid today by a foreign policy that aids the aggressor in Spain,

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shuts its eyes to German aggression in Europe, and fails to offer moral and economic support to the victim of aggression in Asia.

I do not mean, Mr. President, that we should take armed measures in defense of the victims of aggression. On the contrary, it is just because I wish to avoid the necessity of resorting to arms in the future in defense of our own interests that I feel we are making a terrible mistake by pursuing a policy of not helping the victims of aggression through economic measures which are easily open to us and which cannot possibly lead us into serious international complications.

As so often has been stressed, a policy of inaction on the part of the United States is not a program of neutrality. When aggression is rampant a "neutrality" policy such as we have been pursuing does not retard and

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may even facilitate that aggression. As I review our policy in the last few years, I feel that in our foreign policy, characterized chiefly by failure to take a positive stand against aggression, we have step by step been following the lead of the present British Government. The events of the past few weeks convince me that we must break with this lead and resume our exercise of the initiative and again play an independent role. Let England follow us, as she will if we take the lead.

Where can we move most effectively first? The sphere in which the situation is not yet hopeless and in which peaceful action on our part would be attended by the least complications is undoubtedly in the Far East.

I repeat, it is because I wish so much to avoid international conflict, as I know you do, too, that I urge so earnestly the extension of credit to China now,

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before it is too late. It is yet possible for our financial and moral aid to be of decisive help to China. China cannot last much longer without that aid. For the price of a little more than one battleship we can give a renewed vitality to Chinese morale and Chinese effectiveness and deal a powerful blow to aggression throughout the world. To weaken aggression in any part of the world is to strike at aggression everywhere; to help democracy in our part of the world, is to help it everywhere. Must we wait until Japan has completed her conquest before we see what we should have done?

Mr. President, I am taking the liberty of pleading China's cause so earnestly because I know you see the matter as I do and because you have three times told me to proceed with proposals for assistance to China. All my efforts have proved of no avail against Secretary Hull's adamant policy of doing nothing which could possibly be



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objected to by an aggressor nation. I need not tell you I respect Secretary Hull's integrity and sincerity of belief that his course is the right one, but the issues at stake go beyond any one of us and do not permit me to remain silent. It is the future peace and present honor of the United States that are in question. It is the future of democracy, the future of civilization that are at stake. The trade agreements program, so dear to the heart of Secretary Hull, is indeed a force for peace, but I trust you will not think me ungenerous when I say that its potency against the forces of aggression is slight. A substantial aid to China will have infinitely more effect in striking a blow for democracy than trade agreements with half a dozen more countries. What could be so effective a check to aggression, Mr. President, as a successful defense by China? What could strengthen

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democracy more than the emergence of a unified and victorious China? I do not say that our financial aid will bring this about; I say only that without such assistance quickly given, China's chances of defeat are greatly increased.

Mr. President, I beg that you will not let pass this historic opportunity of a first effective economic measure against aggression, this great moral gesture so sorely needed in a world in which "appeasement" has superseded morality. I have never felt more sure of the wisdom of an investment; I have never felt more sure of its urgency.

Mr. President, forgive me if I appear to have learned too well the message you gave in your speech at Chicago on October 5, 1937.

FEDERAL RESERVE BANK  
OF NEW YORK

OFFICE CORRESPONDENCE

DATE October 17, 1938.

CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATIONS WITH  
BANK OF ENGLAND.

L. W. Knoks

Mr. Bolton called me this morning at 11 o'clock. The pound sterling had shown a better tendency this morning, he said, and helped by a market which was suffering from indigestion as a result of the large amount of dollars recently acquired, had gone up to 4.75 9/16. This had enabled him to buy a few dollars. But the moment the New York market opened "tremendous sterling selling orders from New York both for spot and forward delivery" had begun to pile up with the result that sterling had not been able to maintain its improvement. Guaranty Trust, City Bank, Bankers Trust, Central Hanover, Lazard, etc., had been sellers in London and this seemed to disturb Bolton considerably. I offered to check into the matter and call him back a little later.

I called Bolton at 12:55 and reported that my inquiries here had brought out the following facts: there had been some commercial selling in this market today; the movie industry, among others, had sold sterling to two of our banks. Cotton bills on a somewhat larger scale than in the recent past, had been offered to one of them. Stock exchange houses had sold on a moderate scale. All the banks I had consulted had commented on the fact that even for the small offerings that had come into the market there had been buyers "few and far between." Our market was not necessarily bearish on sterling but bewildered and not knowing what to think preferred to hold off. The feeling here seemed to be that Europe in pushing the sterling rate up early today had been a trifle over-optimistic and seemed to have

FEDERAL RESERVE BANK  
OF NEW YORKOFFICE CORRESPONDENCE  
CONFIDENTIAL FILESDATE October 17, 1958.SUBJECT: TELEPHONE CONVERSATIONS WITH  
BANK OF ENGLAND.

L. W. Knoke

2

gone long. Others thought that this morning's improvement could be attributed to the talk of increased armament expenditure here. Sterling might also have received a little support from purchases of gold in India which had to be paid for in sterling.

I am sure Bolton appreciated my making this canvass for him. He had sold, he said, between \$3,000,000 and \$4,000,000 and had done about \$15,000,000 in the form of swaps. This, he said, had enabled him to keep the forward rate for three months down to 1/2 and a little lower.

LWK:KW

RECEIVED  
OCT 21 1958  
FEDERAL RESERVE BANK  
OF NEW YORK

REB

GRAY

London

Dated October 17, 1938

Rec'd 4:25 p. m.

Secretary of State,  
Washington.

1197, October 17, 7 p. m.

FOR TREASURY FROM BUTTERWORTH.

The atmosphere for the moment has changed and the dollar opened offered at 4.73 1/4. During the course of of the day it appreciated to as high as 4.75 1/2 but New York opened a strong seller of dollars and the rate perfected to 4.74 3/8. During the course of the day the British authorities have intervened only on duty to steady the market. Gold fixing was likewise very small: 98 bars being sold at 146 shillings 6 pence. British security markets have continued weak.

In the course of a short conversation Clay, economic adviser to the Bank of England, remarked on the diminution in the pressure on sterling but added that "these spasms temporarily spend themselves but the movement will be resumed" because the Munich settlement is being increasingly regarded as a truce not a peace. Clay went on to say that the United Kingdom could lose a lot of foreign funds  
without

REB

2-#1197, From London, Oct. 17, 7p.m.

without serious domestic repercussions; that after all the gold reserve had been built up against the contingency of foreign withdrawals and therefore there was no reason why it should not be so employed. He obviously was pessimistic about the economic outlook in this country and felt that the incentive for foreign capital to remain in the United Kingdom was diminishing. He had the impression that only a small fraction of the recent movement out of sterling was on behalf of British nationals but that more British money would go to the United States if and when American recovery seemed assured and therefore values on Wall Street were definitely moving upward.

KENNEDY

EMB

ROW

## PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: October 17, 1938, 5 p.m.

NO.: 1767

FROM COCHRAN.

Control tactics were employed to strengthen the franc in London Saturday, (omission) the press stories with regard to alleged decision of the American Treasury to seek renewal of the authority of the President to devalue the dollar to fifty cents and to maintain the stabilization fund, and to the rumors relating to possible devaluation that arose therefrom. Franc recovery today has continued along more natural lines; at a quotation of around 178.68 to .70 the Bank of Franc has been acquiring some sterling. More bids at four francs for three months franc against sterling, but it is suspected that there is artificial support therefor. Continuing gossip of a French exchange guaranteed loan has caused a slight weakening in rentes. The senatorial elections are on October 23; market sentiment is a little more optimistic, since financial circles sense that the Rights may gain at the expense of the Leftists. It is not expected that there will be any decrees until after the elections and perhaps not until after the convention of the Radical Socialists which is to be held at Marseilles shortly thereafter.

I had a telephone call today from Jacobson of the

BIS.

- 2 -

BIS. He told me he is happy to see better business news from the United States, and does not regret the slight dollar weakness resulting from rumors of devaluation and prospective expenditures for armaments; he considers such weakness a very timely aid for sterling, and that in the present circumstances, psychological factors are more helpful in strengthening a currency than are credits. In the long run he believes sterling will gain ground on its own.

Today invoice given by Bank of France to some of New York offices for 165,000,000 francs gold bars for the account of the Bank of England, to be shipped on ILE DE FRANCE.

WILSON.

EA:LWW



## PARAPHRASE OF TELEGRAM SENT

TO: American Embassy, Rio de Janeiro, Brazil

DATE: October 17, 1938, 6 p.m.

NO.: 120

Reference is made to telegram No. 119 of October 13 from the Department.

The Department is informed by the Federal Reserve Bank of New York that the Bank had a telephone conversation on October 14 with the Director of Exchange of the Bank of Brazil and the matter was discussed in detail; thus a cabled reply through the Embassy was not necessary.

HULL.

EA:LWW

## PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Berlin, Germany (part air)

DATE: October 18, 1938, 11 a.m.

NO.: 554

No. 25 FOR TREASURY FROM HEATH.

The newspapers and economic press are full of articles as to the effect on German economy of the acquisition of the Sudeten area but it is too early to predict with any certainty just what the effect of this acquisition will be in the immediate future on Germany's foreign exchange and payment position.

However, at the Economics Ministry and at the Reichsbank it is admitted that the acquisition will intensify the foreign exchange problem for some time to come, but not to a critical extent, it is asserted. So far there has been complete willingness on the part of the Czechs to reach at least a transitional arrangement, whereby the Sudeten industries can continue to export to other sections of Czechoslovakia on a preferential basis, and in return the Czechs can send into the Sudeten area their agricultural and other products on a preferential basis.

A part of the marketing problems of the Sudeten export industries would thus temporarily be solved. However, their competitive ability in markets other than the Czech and German will presumably be lessened by the

artificial

- 2 -

artificial currency conversion rate which is used in the Sudeten region. After the thirty-first of October their labor costs will be raised ~~thruout~~ because of this rate by 40 percent in terms of gold; therefore they will have to increase prices unless they are heavily subsidized at the expense of the rest of Germany.

It was thought by the British that German foreign exchange stringency had recently become more acute since toward the end of September the Exchange Bureau was considerably behind in meeting the exchange demands of German importers of English goods. It appears now that this delay was due merely to a desire to husband foreign exchange resources in view of the possibility of war. During the last few days the German exchange office has filled all past demands for sterling exchange and has met promptly considerable new demands by German importers.

The Reich has published regulations concerning the rate of conversion of Czech currency and debts in Czech crowns in the Sudeten area which are going forward by mail in translation today. Under these regulations the Czechoslovak crown ceases to be legal tender after October 31, 1938, with the exception of Czech notes of 10, 20 and 50 crowns, which for technical reasons will still be acceptable for an un-

- 3 -

stated transitional period. Other denomination notes must be converted before October 31 if the bearer desires to benefit by the artificial conversion rate of one Czech crown equals 12 pfennigs. After that date he will get only the bourse rate which at present is one crown equals 8.6 pfennigs. Debts owed by Sudeten debtors to Czech creditors will be paid through a special exchange adjustment bureau which will shortly be set up at the 12 pfennig rate. On the other hand Sudeten creditors of Czech debtors will have to accept payment of their claims at the 12 pfennig rate.

The financial agencies of the Government are claiming that the new billion and a half reichsmarks loan (see my 16 October 3) will be over-subscribed and that it is probable that a supplementary issue will be made. The subscription period has a week to run.

WILSON.

EA:LWW



DEPARTMENT OF STATE  
WASHINGTON

10-18-32

In reply refer to  
EA

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury and, with regard to the pending transaction between the Federal Reserve Bank of New York and the Bank of Brazil, transmits the following paraphrase of telegram No. 246, October 18, 1 p.m., from Rio de Janeiro:

"Refer to Department's <sup>120</sup>~~128~~, October 17, 6 p.m.

"I am informed by the Director of Exchange of the Bank of Brazil that during the telephone conversation of October 14 the Vice President of the Federal Reserve Bank of New York stated that more time was necessary to study the plan of the Bank of Brazil. The Director added that the Bank would have liked to avoid selling the gold but that it had been obliged to sell it in order to obtain dollar credits to enable continuance of exchange allocation."

A paraphrase of this telegram has also been sent to the Federal Reserve Bank of New York.

~~AA~~

FS

PLAIN

London

Dated October 18, 1938

Rec'd 3:30 p.m.

Secretary of State,  
Washington.

1204, October 18, 6 p.m.

FOR TREASURY FROM BUTTERWORTH.

The volume of trading in the dollar-sterling exchange has not been large; the market does not seem to know which way the momentary trend will go and consequently the rate has moved somewhat erratically. The dollar opened offered at 4.75 and by stages went to 4.76 1/8, then to 4.75 3/4 at fixing. After fixing it has remained steady at 4.75 1/4. 112 bars were dealt in at 146s.2d. which was 1/2d premium. The British fund put in 12 bars and gave something less than 100 bars after fixing.

The franc has been slightly bid with the Bank of France holding the rate at 178 11/16 and acquiring some sterling. The city taking a longer view of the French situation and evaluating France as an ally has not found reassuring the following report which appeared on the ticker this afternoon: "Reports are current in well-informed French political circles today that Daladier is considering the appointment of two additional Cabinet Ministers to

take

FS 2-No. 1204, October 19, 6 p.m. from London

take over two new posts - those of Minister of the Treasury and Minister of Armaments. It is understood that M. Daladier favors the appointment of technical rather than political men for the posts. Meanwhile there is considerable talk in French political circles of the possibility of the Chamber being dissolved early next month and a general election being held some time in December. The belief in parliamentary quarters that a general election is pending is based on the widespread conviction that the Popular Front is a thing of the past owing to the hostility of the Communist Party towards M. Daladier and M. Bonnet. It is also known that the Premier would not hesitate to request President Lebrun and the Senate to dissolve the chamber if he thinks such a step necessary. The only way for the Prime Minister to avoid a general election is in the opinion of many parliamentarians to turn further to the right in building the foundations of his Government majority. The weakness of such a move however lies in the fact that the Centre and Right wing parties are divided among themselves while the Democratic Alliance headed by the former Prime Minister M. Flandin has been badly disrupted by its leader's sympathy with the German point of view during the recent international crisis.

No

FS 3-No. 1204, October 18, 1938, from London

No decision is likely to be reached before the end of this month when the partial elections for the Senate will have been held. From these the Government will glean some indication as to the direction from which the political wind is likely to blow. After this comes the National Congress of the Radical-Socialist Party at Marseilles from October 27th to the 30th, where L. Daladier will have an opportunity of outlining his political programme to the whole party and obtain sanction therefor. Therefore not until November is there likely to be any definite constructive action in political economic industrial or military affairs by the Daladier Government."

The comment here is that Daladier is a bull with the horns of a snail.

CSE

KENNEDY



## PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: October 18, 1938, 5 p.m.

NO.: 1773

FROM COCHRAN.

A little sterling was gained by French control at a quotation 178.68 to 178.70. Better market for French rentes and forward franc. Important holdings of dollars are being liquidated by Bank of Indo-China. Comparative inactivity on exchange and stock markets, as political developments in France are awaited - the senatorial elections, and the financial decrees which must be completed by the fifteenth of November, and the first of which are not likely to appear before the first of November. The refusal of workers in airplane factories to work the prescribed 45 hours on Government contracts in lieu of 40 disgusts the market. If Daladier does not bring out in his decrees some courageous measures requiring sacrifices and inspiring confidence, the market will be genuinely disappointed. Another warning was issued by the Government against rumors as to what the new measures might be. One of those rumors is that Marchandeu will be asked to share the post of Finance Minister with Baudoin of the Bank of Indo-China; according to the rumor, Baudoin would give his expert attention to purely Treasury problems, and Marchandeu would continue to handle the budget. The market

was

- 2 -

was particularly aided today by this rumor.

From Brussels comes a Reuter report that there has been prompt and full subscription of the one billion franc Belgian State lottery loan; this loan was issued in bonds of a nominal value of five hundred francs, with 70 year redemption clause. 485 francs was the issue price, and the rate of interest was to be 3 1/2 percent for the first ten years, and thereafter 4 percent.

END MESSAGE.

WILSON.

EA:LWW

RECEIVED  
OCT 13 1918  
TREASURY DEPARTMENT  
U. S. DEPARTMENT OF THE TREASURY

C  
O  
P  
Y

October 18, 1938.

To: Secretary Morgenthau  
From: Mr. White

The proposal that France build large plane factories in Canada has merit only under the assumption that France cannot (for technical reasons which I would not know) produce all the planes she needs at home during the next few years.

Possibly Mr. Bullitt is in possession of information indicating that is so.

However, on economic grounds the proposal has very little merit. If the only or chief consideration is one of finance, it seems that France would be most unwise to attempt to develop a source of supply for planes in Canada rather than at home.

PROPOSAL THAT THE FRENCH GOVERNMENT ESTABLISH IN CANADA AIRPLANE PLANTS CAPABLE OF CONSTRUCTING SEVERAL THOUSAND PLANES A YEAR.

Conclusion.

The plan has some advantages but these appear at first examination to be much outweighed by the disadvantages:

A. The possible advantages of the plan are as follows:

1. The French Government would have an important source of supply located three thousand miles away from Germany and Italy.
2. France might be able to increase her supply of planes more rapidly by utilizing trained skilled labor of United States and Canada. Were France dependent on the output of foreign owned plants she might not be able to get as many as she would wish, and/or the cost might be higher. Were she to depend on the United States for supplies, those supplies might be stopped in time of war by the application of our "Neutrality Act".
3. It is possible that France might be able to obtain through borrowing abroad a portion of the foreign exchange necessary to construct the plants.

B. The value to France of these advantages is quite uncertain:

1. Inaccessibility of the plant to foreign bombing planes would be an advantage only in war time. But that is the very time when speed, ease, and certainty of delivery of planes becomes important. For France to depend on a source of supply in a foreign country three thousand miles away for so large a proportion of a vital war need would seem to be unwise from a military point of view.
  - (a) Ocean transportation of three thousand miles in war time has its hazards; submarines, mines, air attacks, sabotage, spy activities, etc.
  - (b) Planes manufactured in Canada would be subject to assumption control by the Canadian (or British) government. France would be giving another important hostage to Britain. Canada might decide, in the event of war, that she prefers not to have within her borders an area which might attract

the enemy's bombing planes. Fighting to remain "neutral," Canada might place an embargo on the export of planes to France. Or in the event of a world war she might decide she needs all the airplanes plant capacity available to turn out planes needed for her own protection.

All possibilities considered it would seem that despite her proximity to Germany and Italy, France would have a more dependable supply of planes in war time were they produced at home.

2. Plants with an output of the magnitude proposed would require a large number of trained workers. Where would they come from? The United States itself will absorb all available skilled workers for a long time to come if it embarks on a large program of its own. In fact, there is probably a scarcity of that type of labor now. Large plants built in Canada would greatly accentuate the scarcity, drive up wages still further and complicate our own plane program. Bottle necks of all kinds would develop which would serve only to accentuate price adjustments here.

France would do better, it would seem, to train her own personnel and develop a large scale organization at home.

It is possible that France feels she cannot develop a large scale equipment at home quickly enough, and is afraid to contract for future purchases in the United States both because of the Neutrality Act, and because of the possible interference with production schedules and models by Army and Navy authorities.

This possible interference with a supply from the United States constitutes the chief advantage for attempting to establish factories in Canada as against dependence upon the United States plants. Were the sole alternatives open to France either United States or Canadian sources of supply, the latter might be a little more certain so long as the Neutrality Act remains in force. The importance of that disadvantage is somewhat reduced by the probability that the Act will be modified, or that it would not be permitted to interfere with shipments to France were France to be attacked.

3. France may be able to finance construction of the plants through flotation of foreign loans. Whether Americans could participate directly in such a loan without violating the Johnson Act is not certain, but even if it be assumed that the foreign capital for setting up the plants would be forthcoming from Americans and/or Frenchmen, the chief cost of foreign exchange would remain. The planes produced would have to be paid for

with foreign exchange.

The gold holdings of France are already deemed low, and her balance of payments is already heavily unfavorable. Were France to purchase from abroad several thousand planes a year, the increased pressure on the franc might easily be enough to cause it to depreciate much further.

The suggestion has been made that France would be able to finance the construction with French capital that has already left the country (i.e., flight capital). This is doubtful and even were it true the advantages accruing therefrom are not important. Frenchmen who now prefer to keep their funds outside of France would probably hesitate to invest in any securities which could in the event of war be very easily identified and taken over by the French Government. In any case, the loss of exchange that is most important to the French Government from the foreign exchange aspect is the purchase of the planes and not the cost of the plants.

#### 5. Other disadvantages of the proposal are:

1. For the French people the venture might involve a heavy loss. The expenditure of several billion francs a year at home (especially when financed largely through borrowing) would mean a substantial increase in employment and business activity. Here, however, that amount spent abroad unemployment at home would not decrease and might even increase. Much depends on how the money was raised and on the repercussions on the franc.
2. For the United States the construction and utilization of such a large airplane factory would have some disadvantages difficult to evaluate.
  - (a) It would compete with any large program that might be undertaken by this government, and would add to wage and price maladjustments in the airplane and allied fields.
  - (b) Large plants in Canada might in the hands of a victorious enemy (or of a Great Britain realigned with Germany or Japan in a desperate attempt to save the Empire) constitute a threat to our safety. Possibly, too, important French plane factories near our border would slightly increase the danger of our beinging involved in a European war.

## TREASURY DEPARTMENT

## INTER OFFICE COMMUNICATION

DATE October 18, 1938

TO Secretary Morgenthau  
 FROM Mr. Haas  
 Subject: Government aid to wheat and cotton growers.

Chronological SummaryWheat:

- 1921: Import duty of 35 cents a bushel imposed on wheat. Emergency crop production and seed loans made to farmers in this and succeeding years, a considerable part of them going to wheat growers.
- 1924: Duty raised to 42 cents, the present rate.
- 1929: September -- Supplemental loans of 10 cents per bushel granted to wheat cooperatives. (Market price \$1.27.)  
 October -- Wheat loans granted growers at fixed prices. (Market price \$1.24.)
- 1930: February -- Direct buying of wheat to support prices begun by Grain Stabilization Corporation. (Price \$1.16.)
- 1931: Emergency crop and seed loans sharply expanded. March -- Holdings of Stabilization Corporation reach maximum slightly over 250,000,000 bushels. (Price \$.71.)  
 July -- Stabilization buying program abandoned. (Price \$.465.)
- 1931-32: Liquidation of stabilization holdings begun. Export sales promoted. Sales made to Germany and China under long term credits; and to Brazil in exchange for coffee. (Average price for season \$.55.)
- 1932-33: Liquidation completed. (Average price for season \$.57.)

## Secretary Morgenthau - 2

- 1933-34: (1) Wheat adjustment program inaugurated, financed by processing taxes. Farmers paid \$98,600,000 in rental and benefit payments. Acreage reduced 14.5 per cent. (Season price \$.91.)
- (2) About 16,000,000 bushels of wheat bought to support prices, later distributed for feed and relief purposes.
- (3) Export subsidy provided on 28,000,000 bushels of Pacific Coast wheat to relieve regional surplus, at cost of \$6,500,000.
- 1934-35: Reduction of 12.2 percent in harvested acreage achieved through crop program involving rental and benefit payments of \$101,465,000. (Season price \$1.06.)
- 1935-36: (1) Rental and benefit payments on 1935 crop totalled \$115,368,000. Harvested acreage increased 18.0 per cent. (Season price \$1.00.)
- (2) Federal Surplus Relief Corporation bought 2,600,000 bushels of wheat in Pacific Northwest, which was distributed for relief purposes.
- 1936-37: (1) Rental and benefit payments on wheat merged in general crop program. Acreage decreased 4.6 per cent. (Season price \$1.21.)
- (2) Federal Surplus Commodities Corporation bought 3,000,000 bushels, largely of surplus Pacific Northwest wheat, for relief distribution.
- (3) Export subsidy plan for shipment of flour to Philippines put into operation.
- 1937-38: (1) Acreage increased 31.9 per cent to new high since 1921. (Season price \$1.06.)
- (2) Ever-normal granary plan developed to stabilize supplies and prices.



- 1938-39: (1) Acreage increased 10.3 per cent to new high since 1919. U. S. wheat supply largest since 1932; world supply largest on record. (Price, August, \$.69.)
- (2) A crop loan, made mandatory under new legislation, resulted in loans on 15,177,000 bushels up to October 13, at average of \$.607.
- (3) Heavy purchases of wheat and wheat products made by FSCG for market support and relief distribution.
- (4) Export subsidy plan put into effect on wheat and flour.

Cotton:

1929: August -- Supplemental loans to cooperatives to bring total advances on hedged cotton to 90 per cent of market value; later extended to unhedged cotton at 75 per cent. (Price, 10 markets, 18.0 cents.)

October -- Fixed loan at 16 cents a pound granted to cooperatives. (Price 17.6 cents.)

1930: June -- Cotton Stabilization Corporation granted \$15,000,000 loan to conduct stabilization operations; later took over 1,241,509 bales from cooperatives. (Price 13.2 cents.)

August -- Loan at 90 per cent of market price granted growers through cooperatives. (Price 11.1 cents.)

December -- Market supported by purchase of 78,300 bales of futures by Stabilization Corporation. (Price 9.2 cents.)

1931: November -- Department of Agriculture announced cotton would be accepted at 8 cents a pound as collateral for seed loans; received 400,000 bales under this offer. (Price 5.95 cents.)

## Secretary Morgenthau - 4

- 1932: May -- Farm Board announced beginning of liquidation program. (Price 5.4 cents.)
- July -- 500,000 bales of stabilization cotton donated to Red Cross by Congressional action. (Price 5.5 cents.)
- 1933: (1) Cotton adjustment program inaugurated, financed by processing taxes. Growers plowed up 10,495,000 acres of cotton, for which they were paid about \$179,700,000 in cash and cotton options. (Season price 10.8 cents.)
- (2) Stabilization cotton holdings and cooperative associations holdings totalling 2,381,057 bales, spots and futures, turned over to Secretary of Agriculture for option payments to farmers under plow-up plan.
- (3) Loans made to China and Russia for cotton purchases.
- (4) Under Government 10-cent loan, growers borrowed from Government and private agencies on about 2,400,000 bales.
- 1934: (1) Reduction of 8.6 per cent in harvested acreage achieved by Government payment of about \$115,200,000 in rental and benefit payments. (Season price 12.4 cents.)
- (2) Bankhead Cotton Control Act provided compulsory control of production through 50 per cent tax on sale of cotton over production quota.
- (3) Under 12-cent Government loan, growers borrowed from Government and private agencies on over 4,000,000 bales.
- 1935: (1) Adjustment payment plan adopted to raise incomes of cooperating cotton growers. Total adjustment payments, plus rental and benefit payments on 1935 crop were \$160,200,000. Acreage increased 1.2 per cent. (Season price 11.55 cents.)

- (2) Crop loan below market, at 10 cents for middling 7/8 cotton, brought in only 114,000 bales.
- 1936: (1) Rental and benefit payments applicable to 1936 crop totalled about \$82,000,000. Acreage increased 9.8 per cent. (Season price 12.7 cents.)
- (2) Rise in prices enabled liquidation of substantial part of loan stocks.
- 1937: (1) Rental and benefit payments approximately \$63,700,000. Acreage increased 11.1 per cent. Crop largest on record. (Season price 8.7 cents.)
- (2) Loan at 9 cents, above market level, increased Government holdings by more than 5,000,000 bales.
- 1938: (1) Acreage decreased 22.0 per cent. (August price 8.4 cents.)
- (2) Crop loan, made mandatory under new agricultural legislation, fixed at 8.30 cents. Loans reported through October 17 on total of 1,200,000 bales. Government holds 1,700,000 bales under 12-cent loan of 1934 and 5,200,000 bales under 9-cent loan of 1937, making grand total of 8,100,000 bales.

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### I. Government aid to wheat growers

#### (a) Through tariff action.

(1) Taking the year 1920 as a starting point for this study, the first Government assistance to wheat growers was occasioned by the severe drop in farm prices which began in the fall of that year. To strengthen wheat prices, an import duty on wheat of 35 cents a bushel was imposed under the Emergency Tariff Act of 1921, thereby removing wheat from the free list.

Secretary Morgenthau - 6

(2) Owing to large world supplies of wheat, with the tariff largely ineffective because of our export surplus, prices again reached low levels in 1923 and 1924. To satisfy demands for a higher tariff at this juncture, the import duty was increased by presidential proclamation to 42 cents a bushel, effective April 6, 1924, at which level it has since remained. During half or more of the succeeding years, the production of an export wheat surplus has made the tariff largely ineffective in raising prices.

(b) Under the Farm Board.

(1) On September 5, 1929, the Farm Board announced that supplemental loans on cash wheat, amounting to 10 cents a bushel above the sums borrowed from primary lenders, would be granted to wheat cooperatives through the newly-created Farmers National Grain Corporation. Loans were also to be granted on hedged wheat to bring the total borrowed to 90 per cent of the market price. A limited number of cooperatives was in a position to take advantage of these loans.

(2) More drastic price-supporting action was taken by the Board at the end of October, 1929, when it announced that it would lend growers, through the cooperatives, fixed prices on the various grades of wheat at approximately the market values on October 25. Total net loan commitments to grain cooperatives made by the Board during the year ended June 30, 1930, amounted to \$24,264,000. Of this amount, \$17,912,000 was actually advanced, of which \$9,236,000 was repaid during the fiscal year. Despite the loan program, wheat prices (composite average of 6 markets) declined from \$1.24 in October to \$1.16 the following February.

(3) To provide stronger market support, direct buying of wheat was begun at the end of February, 1930, by the newly-formed Grain Stabilization Corporation, with funds advanced by the Farm Board. Despite this buying program, prices continued downward, reaching the 80-cent level in the early fall of 1930. At that time the Corporation bought heavily of futures contracts, also buying cash wheat at interior and country markets. By the end of the following March, the holdings of the Stabilization Corporation reached a maximum slightly over 250,000,000 bushels. This buying was effective in stabilizing prices around the 70-cent level from November to the end of the season, while declining world prices resulted in putting our prices 25 cents or more above export parities.

Secretary Morgenthau - 7

Prices dropped precipitously to below the 50-cent level at the beginning of the 1931-32 season on the abandonment of stabilization buying. A policy was then adopted, and successfully carried out through this and the succeeding two seasons, of liquidating the stabilization holdings in such a manner as to support domestic prices, largely by sales into foreign consumption channels. As part of this program, wheat was sold to Germany and China on long-term credits, and to Brazil in exchange for coffee.

The selling program tended to strengthen prices. While the price at 6 markets in July 1931 had dropped to 46.5 cents a bushel, the average for the entire 1931-32 season beginning in that month was 55.1 cents, with the domestic crop the third largest on record, and the general price level continuing to decline. In the following season the average price was further raised to 57.0 cents, when the effects of a continued decline in commodity prices and an increased foreign wheat crop were offset by a reduced domestic crop.

(4) In September, 1930, the Farm Board organized and financed a Drought-relief Department of the Farmers' National Grain Corporation, to accumulate stocks of cash grain at certain strategic points to take care of expected demand for feed grains in the drought areas. The expected demand did not develop, and the holdings of this department were liquidated the following spring at a loss of \$789,863.

#### Financial results of stabilization program

It is not possible to separate the financial results of the several price supporting measures taken by the Farm Board, since the wheat accumulated under these measures was eventually merged in the holdings of the Grain Stabilization Corporation.

On June 30, 1931, these holdings amounted to 257,136,571 bushels, after 72,504,481 bushels of wheat previously acquired had been sold. The accumulated wheat was liquidated over a period of several years, the last of it being sold by the end of April 1933.

An approximate estimate of the financial results of the wheat stabilization operations as a whole may be derived from the following data:

Secretary Morgenthau - 8

As of December 31, 1933, there had been advanced to Grain Stabilization Corporation, but not repaid, a total of .....	\$200,951,972
Against this may be credited donations of 95,000,000 bushels to the Red Cross, at cost 1/ .....	<u>119,134,430</u>
Leaving a balance unpaid of .....	81,817,542
Unrealized assets as of that date consisted of:	
(1) 175,442 bags of coffee, which later brought a net return of .....	\$12,734,619
(2) German Government notes 2/ ..	3,961,310
(3) Chinese Government notes 3/ ..	<u>9,212,827</u>
	<u>25,908,756</u>
Leaving an approximate (minimum) net loss of .....	55,908,786, or 17.0 cents per bushel bought.

- 1/ A substantial loss, not indicated, is contained in this figure, since the realizable market value of the wheat at the time of donation was about 20 per cent lower than the cost value.
- 2/ These are now being slowly liquidated, \$50,000 a month being paid against principal and interest. The amount outstanding on October 12, 1938 was \$2,290,640.
- 3/ One \$3,000,000 note sold at face value to Export-Import Bank; remainder fully collected.

(c) Under the Agricultural Adjustment Act.

(1) Direct payments to wheat growers. In 1933 the Agricultural Adjustment Administration adopted production control as its major weapon in attacking the wheat problem. In return for agreements to limit their wheat acreage, farmers were given rental and benefit payments directly from the Federal Treasury, financed during the first years of the program by processing taxes on wheat.

Secretary Morgenthau - 9

Production control, aided by an extended drought in the principal wheat areas, was effective until 1937 in reducing the crop to below the normal domestic requirements, thereby making the tariff effective and maintaining prices at relatively high levels. In 1937, however, an increase in acreage to the highest level since 1921, with yields relatively high, again created a surplus problem. This was intensified in 1938, when a further increase in the domestic crop and the largest world supply on record brought a serious decline in wheat prices.

Total rental and benefit payments to wheat growers applying to the crops of 1933 to 1935, inclusive, were as follows:

<u>Crop of</u>	<u>Rental and benefit payments on wheat</u>
1933	\$ 98,600,000
1934	101,465,000
1935	115,368,000

After 1935 the wheat payments were included in the general farm allotments, and cannot be segregated.

(2) Direct purchases for relief distribution. In the fall of 1933, to supplement the adjustment program, purchases of something over 16,000,000 bushels of wheat were made by the Federal Surplus Relief Corporation, to support and stabilize the grain market after a period of weakness. This wheat was distributed for relief purposes, and the cost, amounting to nearly \$15,000,000, was borne by relief funds.

In the latter part of 1935, a regional wheat surplus in the Pacific Northwest was relieved by the purchase of 2,600,000 bushels of wheat, which was shipped east by rail, largely to the Southern States, to be milled into relief flour.

In 1936 the Federal Surplus Commodities Corporation bought an additional 3,039,000 bushels largely of Pacific Northwest wheat, which was processed and distributed for general relief purposes.

Secretary Morgenthau - 10

In 1938, with the largest supply of wheat since 1932, a more extensive program of relief purchases was embarked upon. Total purchases to the first of September amounted to 21,355,000 bushels of wheat, with additional purchases of wheat cereals and flour bringing the total to the equivalent of about 35,500,000 bushels of wheat.

(3) Export sales under Government subsidies. An export subsidy on Pacific Coast wheat was used in the 1933-34 season to relieve a surplus situation in that wheat region. Through the North Pacific Emergency Export Association, set up in October 1933, export sales of somewhat over 28,000,000 bushels were made between then and the first of August 1934, at prices involving losses averaging about 23 cents a bushel and totaling about \$6,500,000. This program was aided by a loan commitment of \$6,000,000 to the Chinese Government, which imported about 16,000,000 bushels of the total.

In the spring of 1936, \$450,000 was allocated for the payment of subsidies on flour exports from the Pacific Northwest to the Philippines to the end of the fiscal year. This has since been extended each year. The following table shows the flour exports under this plan, in terms of wheat, for each season, with total indemnity payments and average rate per bushel of wheat:

<u>Year ending</u> <u>June 30</u>	<u>Exports</u> <u>bu. of wheat</u>	<u>Total</u> <u>payments</u>	<u>Rate, cents</u> <u>per bushel</u>
1936	862,994	\$159,464	18.5
1937	1,939,316	231,861	11.9
1938	2,148,186	81,255	3.8
1939 <u>1/</u>	1,185,280	98,831	8.3

1/ To October 17, 1938

In 1938, wheat exported under the export subsidy plan to the close of business October 14, according to confidential information from the Department of Agriculture, totalled 12,563,295 bushels, with an average subsidy rate of 11.9 cents per bushel. Flour exported under the subsidy plan through October 17 totalled 457,549 barrels, equivalent to 2,036,093 bushels of wheat. This involved indemnity payments of \$264,197, equivalent to an average of 12.9 cents per bushel of wheat.



Secretary Morgenthau - 11

(4) Crop production and seed loans. A large portion of the funds made available under special appropriations by Congress for emergency crop production and seed loans in eight different years during the period 1921-1931 have gone to wheat and cotton growers, since these areas have frequently been afflicted by drought or other crop disasters. Originally the loans were made by the Department of Agriculture, but in May 1933 this function was transferred to the Farm Credit Administration.

Beginning in 1931, serious crop failures over wide areas, coupled with a breakdown in commercial banking facilities in rural sections, resulted in a considerable expansion in the Federal emergency loan program. Whereas these loans for the entire period 1921 to 1930 had totalled \$15,194,000, the loans in the single year 1931 amounted to \$55,787,000, and in 1932 to \$64,205,000. In succeeding years they declined somewhat, though remaining relatively high compared with the earlier period.

(5) Ever-normal granary plan. In the spring of 1938, the "ever-normal granary" plan was embodied in agricultural legislation applying to wheat. This is essentially an insurance plan for stabilizing growers' incomes, whereby the Government accumulates wheat stocks in normal or large crop years, through crop loans or "insurance" payments, and releases them to growers in years of crop failure.

(6) Crop loan on 1938 wheat crop. Under mandatory provisions of the new agricultural legislation, applying to years of crop surplus, a crop loan was granted to growers on the 1938 crop at a rate slightly above market levels. Loans amounting to \$9,209,636 were made on 15,177,480 bushels of wheat up to October 13, at an average loan price of 60.68 cents per bushel.

#### The present wheat situation

The United States wheat acreage has increased rapidly from the low of 43,400,000 acres harvested in 1934, when it was reduced partly by the crop restriction program and partly by a serious drought. In 1937 the acreage was raised to 64,460,000 acres, highest since 1921, and in 1938 it was increased further to 71,069,000 acres, the highest since the war-stimulated 1919 acreage of 73,700,000 acres, which was the highest on record.

The world wheat supply for the 1938-39 season is the highest on record. The total United States supply of 1,094,301,000 bushels compares with 957,207,000 bushels in the previous season and is the highest since 1932.

Secretary Morgenthau - 12

## II. Aid to cotton growers

### (a) By tariff action

Though the possible benefits to cotton growers from import duties on cotton are very limited, since imports are confined to relatively small quantities of extra-staple cotton, the Emergency Tariff Act of 1921 imposed a duty of 7 cents a pound on cotton having a staple length of 1-3/8 inches or more. This was removed in the Act of 1922. In the 1930 Act a duty of 7 cents a pound was again imposed, and extended to staple lengths down to 1-1/8 inches.

### (b) Under the Farm Board

#### 1929

(1) A cotton loan plan was announced by the Farm Board in August 1929, providing supplemental loans on hedged cotton to qualified cooperative associations sufficient to bring total advances to 90 per cent of the market value. In September this was extended to provide a total advance of 75 per cent on unhedged cotton.

(2) A more definite market-support measure was adopted in October, to counteract price weakness, when fixed loans at 16 cents on middling 7/8 inch cotton (slightly under the prevailing market) were granted to growers through cooperative associations. Advances of \$18,500,000 were made on this basis.

#### 1930

(1) A serious price decline in the first half of this year, reaching 13.2 cents (10 market average) in June, resulted in formation of the Cotton Stabilization Corporation, with an initial fund of \$15,000,000, to conduct stabilization operations under the Agricultural Marketing Act. Soon afterward it purchased the unsold stocks of cotton cooperatives, amounting to 1,241,509 bales, and held them off the market.

(2) Prices continued to decline. A 90 per cent loan with 3-year maturity, granted to cotton growers through the cooperatives in the fall of 1930, did not prevent a price decline to 9.2 cents in December of that year. Cotton loans totalling \$85,921,000 were approved by the Board during the 1930-31 fiscal year.

Secretary Morgenthau - 13

(3) As the result of a 2-cent price decline between November 1 and December 15, the Stabilization Corporation entered the futures market in November and December to stabilize prices, buying 78,300 bales of futures, which were later converted into spots.

#### 1931

(1) In return for an agreement of Southern banks to finance the holding of not less than 3,500,000 bales, the Board agreed to hold stabilization stocks of 1,300,000 bales off the market, and to continue to finance 2,100,000 bales held by cooperatives until the end of the season.

(2) The Department of Agriculture agreed to accept cotton as collateral for seed loans at 8 cents a pound (market price 5.95 cents), receiving 400,000 bales under this offer.

#### 1932

(1) The liquidation of stabilization stocks was begun, with announcement in May that not over 650,000 bales (about half the stock) would be sold during the next season.

(2) In July, Congress turned over to the Red Cross 500,000 bales of stabilization cotton for relief purposes. Part of this was used by the Red Cross to pay the costs of processing and transporting the remainder.

(c) Aid to cotton growers under the Agricultural Adjustment Administration.

#### 1933

(1) Under the new plan of attacking the cotton surplus problem through Government subsidies for acreage reduction financed by processing taxes, the Secretary of Agriculture took over the small remaining cotton holdings of the Stabilization Corporation, plus cooperative association cotton held as security for loans, and seed and production loan cotton, amounting in total to 2,381,057 bales of spots and futures. This was pooled, and option certificates issued against it were used as part-payment to growers for plowing under part of their crop.

Secretary Morgenthau - 14

(2) The plow-up program resulted in a cut in the cotton acreage of about 10,495,000 acres, equivalent to somewhat over 4,000,000 bales. The total cost to the Government of the 1933 program is estimated at about \$164,600,000, divided as follows:

Cash rental payments	\$112,940,000
Option cotton	48,840,000
Administrative field costs	<u>2,820,000</u>
	\$164,600,000

(3) A crop loan at 10 cents for middling 7/8 cotton (about a cent above market prices) was announced in the early fall. About 2,400,000 bales were pledged with the Government and private agencies under this loan, part of which was liquidated when prices rose to above 12 cents later in the season.

(4) Exports of surplus cotton were facilitated by loans to foreign governments through the Reconstruction Finance Corporation. The Chinese Government borrowed \$8,291,222 for the purchase of cotton, and some 75,000 bales were exported to Russia under similar loans.

#### 1934

(1) Difficulty with non-cooperating growers led to passage of the Bankhead Compulsory Cotton Control Act in 1934, assessing a penalty of 50 per cent of the market value on cotton sold in excess of production quotas.

(2) The cotton acreage was reduced to 27,860,000 acres planted (compared with a previous 10-year average of about 43,900,000), at a cost to the Government in rental and benefit payments of \$115,200,000.

(3) A crop loan of 12 cents for middling 7/8 cotton, somewhat below the early-season market level, proved too high in view of later developments. More than 4,000,000 bales of the 9,636,000-bale crop went into the loan, tending to disrupt normal price relationships and to interfere with domestic and export merchandising.

Secretary Morgenthau - 15

1935

- (1) The cotton acreage planted in 1935 was held down to 28,197,000 acres, an increase of 1.2 per cent over 1934.
- (2) An "adjustment payment" plan was adopted, whereby selling prices on growers' production quotas were raised to the equivalent of a 12-cent level for middling 7/8 cotton at the 10 designated spot markets. The adjustment payments plus rental and benefit payments applicable to this crop totalled \$160,200,000.
- (3) A crop loan was offered at 10 cents for middling 7/8 cotton. Being substantially below the market, it brought in only 114,000 bales.

1936

- (1) The acreage in this year was increased 9.8 per cent, with rental and benefit payments totalling about \$82,000,000.
- (2) A substantial part of the loan stocks from previous crops was liquidated on the price rise which began late in the year and continued into the spring of 1937.

1937

- (1) The acreage in this year was increased by 11.1 per cent, with rental and benefit payments approximating \$63,700,000. The crop produced on the increased acreage was the largest on record.
- (2) A loan at 9 cents, which proved to be above the market level, increased Government holdings by more than 5,000,000 bales.

1938

- (1) The acreage this year was decreased 22.0 per cent, with rental and benefit payments yet to be determined.
- (2) A crop loan, made mandatory under the new agricultural legislation, was fixed at 8.30 cents, somewhat above the market level. Reports received through October 17 show loans by Government and private agencies to date on 1,200,000 bales.

Secretary Morgenthau - 16

The present cotton situation

The cotton acreage has increased gradually from a low of 27,860,000 acres in 1934, reaching a peak of 34,471,000 acres in 1937, which was still somewhat below the levels immediately before application of the agricultural adjustment program. The average yield per acre, however, has shown a great increase. In 1937 a yield far above any previous record resulted in a new record crop of 18,946,000 bales. Prices declined from a season average (at 10 markets) of 12.7 cents in 1936-37 to 8.7 cents in 1937-38. Despite a 35.5 per cent reduction in the crop in 1938, the price in August was down to 8.4 cents. The Government loan at 8.30 cents has stabilized spot prices and supported near-month futures. Cotton for October 1939 delivery is now quoted in the futures market at around 7.60 cents.

The carryover of American cotton in the world on July 31 reached a new high record of 13,652,000 bales, which compares with a previous peak in 1932 of 13,263,000 bales. In the interval, however, the world consumption of American cotton has declined, largely because of an expansion in the production and use of foreign cotton. In 1931-32 the world consumption of American cotton was 12,528,000 bales, while in 1937-38 it had declined to 10,930,000 bales. Exports by this country during the current season through the week ended October 8 were 691,000 bales, as compared with exports of 970,000 bales during the same period last year.

Reports received through October 17 show loans made under this year's Government loan plan on 1,200,000 bales. The Government holds 1,700,000 bales under the 12-cent loan of 1934 and 5,200,000 bales under the 9-cent loan of 1937, making a grand total of 8,100,000 bales to date.

Members of Industrial Committee of  
National Resources Committee

10/18/38

f Mr. Louis Bean — Economic Adviser to A.A.A.  
(Alternate) Room 218 Administration Bldg., Dept. of Agriculture.  
Br. 340

ok ✓ Mr. Thomas C. Blaisdell, Jr. — Director, Monopoly Study, Securities  
and Exchange Commission.  
Room 806, S.E.C.  
Br. 399 and 400

✓ Mr. Mordecai Ezekiel — Economic Adviser to the Secretary of Agriculture  
Room 218 Administration Bldg.  
Br. 314

✓ Mr. Leon Henderson — Executive Secretary, Temporary Economic Committee  
Apex Building, Room 281.  
Br. 399, Federal Trade Commission

✓ Mr. Lauchlin B. Currie — Assistant Director, Div. of Research & Statistics,  
Board of Governors, Federal Reserve System, Rm. 3230.  
Br. 305

✓ Mr. Charles W. Eliot, 2nd — Executive Officer, National Resources Com.  
Room 6137, Interior Bldg., North.  
Br. 3832

f Mr. A. F. Hinrichs — Chief Economist, Bureau of Labor Statistics  
(Alternate) Room 2317, Dept. of Labor  
Br. 237

✓ Mr. Isador Lubin — Commissioner of Labor Statistics  
Room 2311, Dept. of Labor  
Br. 303

✓ Mr. Gardiner C. Means — Director, Industrial Section, N.R.C.  
Room 6123, Interior Bldg., North  
Br. 3403


*White*

*Supper Sunday Oct  
7:30 Home  
P.O.*  
10/23/38

October 18, 1938.

October 18, 1938  
Tuesday

Mr. Lochhead reminded Secretary Morgenthau that the Spanish Ambassador had requested that we make a bid for another lot of silver as soon as convenient. Secretary Morgenthau authorized the placing of a bid for 10,000,000 ounces of silver through the Spanish Ambassador and this bid was transmitted to the Ambassador by Mr. Bernstein and Mr. Lochhead at 12:30 noon today.





(CONFIDENTIAL)

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**STRICTLY CONFIDENTIAL**P A R A P H R A S E

A telegram (No. 1347) dated October 18, 1938, from the American Consul General at Shanghai, reads substantially as follows:

The Japanese are concerned lest silver valued at about Chinese \$40,000,000, located in a Chinese bank in the French Concession at Tientsin, and about \$14,000,000 held by a Chinese bank located in the British Concession, be shipped out of the port of Tientsin. There has been much friction and difficulty at Tientsin in regard to this silver, according to information supplied to the Consul General confidentially by the Commercial Counselor of the British Embassy. The British Embassy is thinking of proposing, as a temporary solution of this problem, that the silver stocks be placed under seal with the approval of the Japanese authorities and the Chinese banks. Before taking this step, however, the British Embassy would like to know whether the Government of the United States has any interest in this silver or its possible purchase. The Commercial Counselor of the British Embassy indicated that an interest by the American Government in this silver or its purchase might affect their decision as to whether or not to make the proposal as outlined above. The Consul General told the Counselor that he was not informed in regard to this matter but that he would make inquiries. The Consul General desires to know the nature of the reply which he should make to the British Embassy.

## RADIOGRAM

U S S Canopus  
(Hongkong)  
October 18 1938

URGENT

Seahn DU

Far Nicholson - Japanese force of about ten thousand advancing from Chong-Mak-Tau to Fu-Min-Chai (latter just above Bocca Tigris forts in Pearl River delta). Has intention apparently to open Pearl River boom to permit Japanese naval vessels now concentrating Namtai to proceed up the river to Canton. General Mok-Rei-Tak commander Bias Bay area reported executed for failure produce adequate defense. United Press have just received London inquiry in connection with bond holders of Kowloon-Canton railway Chinese section and their inquiry of manager Jardine Matheson who have interest operations of railway and bonds thereof brought forth answer that bond holders were amply protected. This very significant for about four months ago Chinese authorities approached Britain in regard to purchase entire controlling stock Kowloon-Canton railway. Implication is that Britain has arrived at understanding with Japanese re operation Kowloon-Canton railway following completion Japanese invasion of South China. Yesterday I took tour with Colonel Holt of British border and there appears no excitement that quarter. No more than three hundred troops stationed there more to aid police with refugees than anything else. Letter coming into Hongkong slowly at rate of about two hundred per day. So far Chinese not making much show against invaders. Some British authorities predict the fall of present Chinese Government after Hankow and Canton fall with H H Kung out and T V Soong in along with Eugene Chen and General Pei Chung Hsi. Soong and others very silent about present situation and appear to be uninformed in regard to southern defense program.

CAMPBELL

RECEIVED

OCT 18 1938

ARMY DEPARTMENT

RECEIVED IN THE OFFICE OF THE SECRETARY OF WAR

13668

WORKS PROGRESS ADMINISTRATION

Estimated Net Total Number of Households  
and Persons Receiving Relief and Emergency  
Employment on Federal Work Programs  
September 1938

190

10-19-38

12451

The net total number of recipients of public relief and employment on Federal work programs increased slightly between August and September 1938, the change amounting to less than 1 percent. According to preliminary estimates, 21,947,000 persons, or approximately 17 percent of the population of the continental United States, were aided during September. It is estimated that these persons were members of 6,854,000 households.

The accompanying tables present monthly estimates for the period January 1933 through September 1938 and a distribution by separate programs for the month of August 1938. Allowances have been made in these estimates for duplication between programs. The results are necessarily approximations and subject to revision.

The estimates cover all households and persons benefiting from the general and emergency relief programs financed in part from FERA and in part from State and local funds; rural rehabilitation advances made from FERA funds and subsistence grants made by the Resettlement Administration and later by the Farm Security Administration; the three special assistance programs of the Social Security Board and other programs of these types conducted by state and local agencies without Federal participation; employment of all relief and non-relief persons on projects conducted under the Civil Works Program, Civilian Conservation Corps, National Youth Administration

13668

- 2 -

(including the student aid program), Works Progress Administration including employment of persons paid from funds contributed by state and local sponsors, and Federal agency projects financed by transfer of WPA funds; Public Works Administration and Bureau of Public Roads projects; and employment on all other Federal work programs financed in whole or in part by emergency appropriations of Federal funds.

The estimates do not include allowances for administrative employees, recipients of unemployment compensation, institutional care, surplus commodities, rural rehabilitation loans made by the Resettlement Administration and Farm Security Administration, or regular Federal construction employment other than public roads employment.

Works Progress Administration  
October 19, 1938

## WORKS PROGRESS ADMINISTRATION

ESTIMATED NET TOTAL NUMBER OF HOUSEHOLDS AND PERSONS  
RECEIVING RELIEF AND EMERGENCY EMPLOYMENT  
ON FEDERAL WORK PROGRAMS

January 1933 through September 1938

Continental United States

(000 omitted)

	Households	Persons		Households	Persons
<u>1933</u>			<u>1936</u>		
January	4,656	18,283	January	6,091	20,714
February	4,976	19,565	February	6,249	21,308
March	5,472	21,537	March	6,248	21,267
April	5,361	21,113	April	6,015	20,435
May	5,237	20,719	May	5,818	19,455
June	4,868	18,919	June	5,607	18,597
July	4,570	17,365	July	5,452	17,942
August	4,396	16,992	August	5,558	18,300
September	3,996	15,162	September	5,629	18,620
October	4,142	15,688	October	5,898	19,006
November	5,455	19,973	November	5,966	19,165
December	7,101	24,946	December	5,926	18,925
<u>1934</u>			<u>1937</u>		
January	7,855	27,578	January	5,959	19,166
February	7,916	27,749	February	5,920	18,775
March	7,201	25,613	March	5,956	19,001
April	6,326	22,639	April	5,886	18,480
May	5,757	20,954	May	5,696	17,648
June	5,698	20,716	June	5,428	16,899
July	5,944	21,615	July	5,029	15,331
August	6,165	22,459	August	4,812	14,515
September	6,165	22,259	September	4,734	14,128
October	6,276	22,409	October	4,880	14,324
November	6,444	22,953	November	5,024	14,801
December	6,598	23,672	December	5,337	16,114
<u>1935</u>			<u>1938</u>		
January	6,779	24,211	January	5,836	17,815
February	6,702	23,965	February	6,166	19,060
March	6,677	23,704	March	6,528	20,369
April	6,656	23,451	April	6,653	20,914
May	6,584	23,054	May	6,783	21,338
June	6,265	21,898	June	6,771	21,477
July	6,038	21,136	July	6,701	21,388
August	5,987	20,748	August <sup>A/</sup>	6,805	21,761
September	5,597	19,247	September <sup>A/</sup>	6,854	21,947
October	5,631	19,083			
November	5,553	18,746			
December	5,893	20,124			

<sup>A/</sup> Preliminary

October 19, 1938

Preliminary

## WORKS PROGRESS ADMINISTRATION

Estimated Net Total Number of Households and Persons  
Receiving Relief and Emergency Employment on  
Federal Work Programs During August 1938  
By Programs  
Continental United States

(000 omitted)

Agency or Program	Administrative Reporting Units		Households	Persons
	Unit	Number		
Works Progress Administration <u>A/</u>	Employees	3,124	3,124	12,353
General Relief	Cases	1,608	1,608	5,105
Civilian Conservation Corps	Employees	328	316	1,226
Aid to the Aged, Blind, and Dependent Children:				
Old-age assistance	Recipients	1,720)		
Aid to the blind	Recipients	64)	1,871	3,403
Aid to dependent children	Families	266)		
Farm Security Administration Grants	Grant Vouchers	60	60	300
Student Aid	Employees	2	2	2
National Youth Administration Work Projects	Employees	219	219	235
Other Federal Agency Employment under E.R.A. Acts	Employees	178	178	628
Emergency Employment of Federal Agencies under Other Acts	Employees	128	128	384
<b>NET TOTAL <u>B/</u></b>			<b>6,805</b>	<b>21,761</b>

A/ Includes the estimated number of employees paid by sponsors.

B/ Does not equal the sum of the totals shown for individual agencies and programs because allowance has been made for duplication.

October 19, 1938

## RE CHINESE TUNG OIL ARRANGEMENT

October 19, 1938.  
9:30 a.m.

Present: Mr. Hanes  
Mr. Taylor  
Mr. Oliphant  
Mr. Foley  
Mr. Lochhead  
Mr. Gaston  
Mr. Haas  
Mr. McReynolds  
Mr. Lawrence Morris (for brief period)

McR: Well, Wayne, I guess this is your party. You better sit in the boss's seat.

Taylor: Uh-uh, I'm just a consultant in this one.

McR: I've never been able to find out who was anything but a consultant on this damn thing. I think the boss is trying to find out himself.

(Oliphant, Hanes, Foley,  
and Gaston come in)

Hanes: Wayne, you didn't talk to Harry White after he talked with Austin of W. R. Grace and Company?

Taylor: Haven't seen Harry White for ....

Oliphant: Six months.

Taylor: No, it isn't that long, but it's four days, I guess. When was it, Friday - I think maybe Saturday I saw him.

McR: No, he was supposed to be at the boss's house in the country on Saturday.

Gaston: Monday.

Haas: Monday, 11 o'clock.

Taylor: Friday was the last time I saw him.

Haas: He asked for a day off in New York - Tuesday - so he's still there.

Gaston: He was to spend yesterday in New York.

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- Taylor: Just what I thought, George. I mean you turn an economist loose in a big city like that, no telling when he's going to show up.
- Hess: More problems there than in the economic field.
- McC: Yes. Night snows too.
- Oliphant: Well, who knows where we stand on the transportation thing now?
- Lockhead: Well, I don't know anything more than what the Chinese said to me when they were in the other day, dropped in. They said they'd seen some of the truck people, and I think it was their idea that their first purchase would be with General Motors because General Motors fellows were willing to snoot a fellow right over on the boat and start it. But they've set aside two million dollars ....
- Oliphant: Well, on the legal side of it, their lawyer, Lawrence Morris, has organized the corporation. In fact, the papers have been filed, the corporation is in existence. Nobody knows it and nobody ever will know it, because it's the International Trading Corporation, the incorporators of whom are ....
- Foley: ... dummies. Universal - sounds like a moving picture company.
- Hess: Universal Trading Corporation.
- Oliphant: Universal.
- Hess: Not Chinco.
- Lockhead: Can change the name to Chinco any time, can't you?
- Foley: Any time. Very simple procedure.
- Lockhead: You can make it the Universal Chinco if you want to.
- Oliphant: But Lawrence said they were sort of reticent when they were up to see him Saturday.
- Hess: Is that Dave Morris's boy, or Henry's?



Foley: Dave's boy.

Lochhead: You have him out here (in reception room).

Foley: Yes.

Hanes: Where is he - is he in your office, Ed - work there?

Foley: He's a partner of Hawkins, Delafield, & Longfellow.

Oliphant: He's apparently counsel ... (further words not understood).

Hanes: Oh, I see, they've been doing it. I haven't seen him around here before.

Foley: No, they retained him, you see, to do their legal work for them.

Oliphant: I think we did a pretty good job of picking him, don't you, Ed?

Foley: Well, I think you were pretty largely responsible for that, but I think it was a good job. Couldn't get a better person to do it. He's got his father interested in it. His father met them when they were up there on Saturday.

Hanes: Dave?

Foley: Yes.

Oliphant: Say, Ed, Lawrence didn't make any progress with them on the selection of the real operators, did he?

Foley: No, no, they didn't open up at all on that end of it.

Lochhead: The real operators of the company - I tell you one thing you're going to run into there. We better have this Lee in on this.

Oliphant: Better have what?

Lochhead: Lee.

Taylor: K. C. Lee.

Lochhead: K. C. Lee. You know, he's a fellow with some trading company in New York - Chinese trading company. Darn smart fellow, this fellow Lee.

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Oliphant: Chinaman?

Lochnead: Chinaman. Does a lot of buying for the Chinese. But probably ... (makes palm-rubbing gesture) ... pretty good squeeze when he's around. And he's pretty close to Kung.

(Phone rings)

McR: (On phone) Hello.

H.M.Jr: Hello, Mac. I hadn't intended to talk to the crowd, but as long as I'm on the phone I will.

McR: Why, I understood yesterday you wanted to talk to them about that tung oil stuff.

H.M.Jr: Well, I wanted them to put all their cards on the table, and I wanted to do some business. I don't know just where all the ends are.

(Dictaphone-recorded conversation follows:)

Wednesday  
October 19, 1938  
9:43 a.m.

HMJr: - choice of one or two alternatives and so would the Chinese.

William H. McReynolds: Well, ah - ah - they're all here - do you want to talk to - ?

HMJr: No, I don't want to talk. When I come down Thursday I want to say - have them say, "You can do it - here's plan A, B and C; any one of the three plans will work. Ah - The following plan is the best from the standpoint of the paint and varnish - or the Chinese or the Government." I want the thing sewed up.

McR: All right.

HMJr: And I - I don't want to have to do it all myself.

McR: O. K. I'll ah - ah -

HMJr: I mean we sit around and nothing happens. Now, ah - these people are beginning to move their tung oil. Are we going to buy it or who is going to buy it? - How are we going to finance it and all the rest of the stuff.

McR: Well, I understand that that - ah - this corporation has been formed and they're ready to go.

HMJr: Well, I mean - but from the Chinese standpoint - where are they?

McR: Yes. Well -

HMJr: I mean who is going to buy it - who is going to buy the tung oil?

McR: (Speaks to group in Secretary's office: Ah - the Boss wants to know who is going to buy the tung oil. Does anybody know? (Short pause) Ah - suppose you talk to him, Johnny, a minute.) Ah - just a minute, I think Johnny

HMJr: Hello.

John Hanes: Hello, Henry - John Hanes.

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HMJr: Yeah.

H: Ah - the program so far as we've gone with it just contemplates the American Corporation ah - making a contract with the Chinese Government.

HMJr: Yes.

H: The Import and Export Bank to lend the American Corporation the money and that Corporation in turn will give a contract to the American varnish manufacturers. Now, that's as far as we've gone - that's a rough outline of it and - there may be some other way of doing the thing that might be better - I don't know.

HMJr: Now just say it again, John.

H: The - the American Corporation has been formed and that's already been registered in Albany.

HMJr: Chinco?

H: That - no - well, that's going to - it's called momentarily, The Universal Corporation.

HMJr: All right.

H: That corporation will make a contract with the Chinese Government -

HMJr: Yes.

H: - for the delivery of this tung oil at C. I. F. San Francisco or -

HMJr: Yes.

H: - New York.

HMJr: Yes.

H: Ah - the next step would be that the Import Export Bank would loan to someone, either an intermediary or to this American Corporation.

Operator: Hello.

HMJr: Yes.

O: Hello, Mr. Morgenthau?

HMJr: Yes.

O: May I speak to you a moment, please?

HMJr: Yes.

(Short pause)

HMJr: - a minute.

O: All right.

HMJr: Hello.

O: Go ahead.

John  
Hanes: Hello.

HMJr: Go ahead, John.

H: Ah - you - we got up to the point where the ah -  
American Corporation had borrowed money or through  
an intermediary had borrowed money from the Import  
Export Bank.

HMJr: Yeah.

H: Then the next step would be to make a contract with  
the American paint and varnish trade, either with  
the individuals who already have machinery for this  
operation in China - there are two corporations -  
the Archer-Daniels Midland Company and the Spencer  
Kellogg Company both of whom have big investments,  
as we understand it, in China for the transportation  
of this oil.

HMJr: Well, John.

H: Yes, sir.

HMJr: Will you and the people in the room there push this  
thing forward now just as fast as we can so it gets  
down to a point that I can say yes or no and the  
Chinese can say yes or no and the paint and varnish  
people, see?

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H: That's right.

HMJr: In other words let's go to town on it and let's try to clean it up this week.

H: Well, I think the thing to be cleaned up is - the only thing that I see is - is the transportation problem. -

HMJr: Well -

H: And we haven't got that cleared yet.

HMJr: They're already moving this tung oil; the first shipment's on the water.

H: Yes. Well, we - so far as we're concerned here - I think we've got a pretty clear idea of how the thing can be done. Now - it's a question now as to whether the Chinese can come through with the tung oil - I think everything else would be -

HMJr: Yeah, but we have no - we have -

H: We have no contracting parties in this country agreed but we have stayed away from that purposely because we didn't want to make a deal with the wrong ones and we didn't want to go too fast with it until we knew exactly where we stood.

HMJr: Well, what I'm saying - now, try to go to town on it, will you?

H: All right. We'll get the - we can get the paint fellows down here for Friday. I think we'd better make it Friday instead of Thursday because we would rather lay this before you before we get them down here.

HMJr: That's right.

H: All right. Fine.

HMJr: Thank you.

H: Do you want to say anything else to them?

HMJr: No, thank you.

H:           They're all here.  
HMJr:       No, thank you.  
H:           All right.    Goodbye.  
HMJr:       Goodbye.

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- Oliphant: I move that John Hanes be elected chairman of the tung oil committee.
- Taylor: He's it.
- McK: Seems to be already. He seems to be it already.
- Oliphant: Well, I mean this thing is sort of floating around. Is White handling it or am I handling it or are you (Hanes) handling it, so forth.
- Gaston: I think the Secretary has given John a direct commission now to head up this thing.
- Hanes: Well, it seems to me the first thing we've got to find out is to find out with whom this corporation is going to make a contract, because that contract has got to be the hypothecation of the arrangement with the Export-Import Bank. Isn't that right, Wayne?
- Oliphant: Well, Henry mentioned the other day to me - the idea is likely to come back to him Thursday - the desirability of the Export-Import Bank making the loan to the varnish people, as opposed to making the loan to the Universal Trading Corporation.
- Hanes: That brings up the question ....
- Taylor: I don't think there's very much in that.
- Hanes: That brings up a question which you all can answer a damn sight better than I can, because I don't know. Is it possible, or would it be feasible to loan - for the Export-Import Bank to make a loan direct to a group of private importers? Would that be good politics, would that stand up?
- Oliphant: Well, they'd be individual loans. It's perfectly legal to.
- Hanes: I'm thinking now in terms of the politics of it. Would it be good business from our standpoint to enter into a ....
- Oliphant: Well, I think Henry had in mind it would be better politics than loaning direct to the Chinese outfit.



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Lochhead: Would these individuals in turn loan to the Chinese?

Oliphant: No, they'd pay cash.

Hanes: We can't loan - as I understand it, we can't make a loan without interfering with some State Department - as Henry said, we can't make a loan direct to the Chinese under any consideration, so it would seem to me the Americans have also got to form a corporation, you see. - If we could get ....

Oliphant: No, John, they can't because of the Sherman Act. See, we've got to watch that. And the way we're handling that - Ed, correct me if I'm not right - this corporation, this Universal Corporation would go out and offer this tung oil, make it available to these various users, on the same percentage basis as their consumption during the previous year. And then we avoid cutting out the middleman by providing that they will handle it in the usual way, but handle it on a commission basis. Isn't that the way they worked it?

Foley: That's the way I understand it, yes, sir.

Oliphant: To avoid this being a combination of American business men fixing the price of an import article, which is especially prohibited by a statute dealing with imports.

Hanes: That would mean, then, that each American manufacturer would have to make his contract with Chinco.

Oliphant: That's right.

Hanes: After we in turn had made a loan to Chinco.

Oliphant: Now, if we make a loan to Chinco and it's a question of financing this inventory - now, that inventory can be financed by either the first name on the paper being the American consumer, the American varnish manufacturer, or Chinco.

Taylor: Has to be Chinco.

Oliphant: What?

Taylor: Has to be Chinco. You never can get your American manufacturer on that paper.

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- Hanes: Well, as I understand it, if we put the American manufacturer on there, we would be putting three - say, Grace, Daniels, and Kellogg, who have between them about 80 percent of the import of this article - that we'd be putting those three together and we'd be aiding and abetting in the violation of that statute then, wouldn't we?
- Oliphant: Well, let's forget Export-Import. Suppose the varnish manufacturer says, "I've decided to lay in a big stock of tung oil and I want some credit with which to finance that inventory," and he goes to Jesse Jones and Jesse Jones makes him a hundred thousand dollar loan. It's an inventory loan, see? And when he gets the cash he turns that over to Chinco. Now I'm talking about the possibility now, see?
- Lochhead: (Nods doubtfully)
- Oliphant: Now, if they do that individually, that doesn't involve any violation of the Sherman Act. So it is purely a question of policy as to whether or not you want your loan made to Chinco by Export-Import Bank or made by Export-Import Bank to the users.
- Hanes: Well now, let me ask you another question.
- Lochhead: Not going to get the Americans in, because it's a question of making advance payments, and if we lend him money to do that we'd have to have them on the paper, and they in turn would be holding the bag to make the loan to China, and they're not going to do it.
- Taylor: They haven't got any inventory until they get it. When they do get it, they don't have to be financed for it.
- Hanes: You can lend them money without recourse.
- Taylor: They don't need to be financed for those inventories.
- Hanes: The American people.
- Taylor: No.
- Oliphant: They do in effect if Chinco is not financed.

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- Taylor: Well, if I were running Archer, Daniels, Midland, why, I wouldn't see any necessity for being financed for that one, outside of my ordinary business.
- Oliphant: That's because you're assuming you can get tung oil in ordinary course.
- Hanes: Of course, the Archer, Daniels, Midland - this stuff is laid down on seaboard, and it's shipped to Archer, Daniels, Midland, against documents. They pay for it and take it out; that money goes right to Chinco and is turned over to Export-Import Bank in repayment of the loan.
- Oliphant: You're now talking about spot oil. That isn't what we're talking about. What we're talking about is that Archer, Daniels have decided they're going to secure themselves a future supply of oil at a stable price, a three-year supply of oil at a stable price. And they find that that can't be obtained without giving the money to the seller in advance. Now, in order to give the money to the seller in advance, they've got to get that money from some source. Now of course, they're not going to hold the bag; you're right that they're not going to hold the bag. So if the advance is made to them, it's going to be an advance like to the farmer for corn, an advance without recourse. But it can be made either to them or Chinco.
- Hanes: That's fine up to that point. Let me ask you a question right there. Do we want to deal with one company? That's question one.
- Oliphant: I just used them as an example. A whole series would do the same thing.
- Hanes: Suppose we want to deal with these companies we've been dealing with that hold 80 percent of the business at the moment. Can we make a deal with those four people, saying just what you said about one? Can we translate that into terms of four, without getting them into violation of the Anti-trust Act?
- Oliphant: (Nods yes)
- Hanes: We can? All right.

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Oliphant: Chinco says, "We're here ready to sell the oil," and Jesse Jones or Export-Import Bank says, "We're here ready to loan the money on this oil."

Now, I haven't expressed my position, my own thought, about which is the better from the standpoint of policy. I think it is much better to have the advance made to Chinco, for this reason: that if you don't you've got a lot of scattered little users and it's going to be an awful looseness to try to finance those fellows.

Hanes: I agree, but there ....

Oliphant: I think you could work it out for the three or four big users.

Hanes: Does that bring us into conflict with the State Department, because whereas you are not lending money to the Chinese Government, you are lending money in a roundabout way to the Chinese Government.

Oliphant: No, I don't think so.

Hanes: You're lending to the American corporation.

Bochhead: Incidentally, Mr. Oliphant, if we lent money to the Universal, could you get a guaranty of the Chinese Government on that paper of the Universal Corporation without its interfering with State Department? I mean the lending to the Universal would be really lending to the Chinese Government. We want a guaranty.

Oliphant: I don't understand this interfering with the State Department. My understanding was that the State Department was inclined to let this tung oil go through if the thing wasn't done too explicitly; so long as the Export-Import Bank handled it, and so forth, they had no objections.

Hanes: Well now, Henry told me ....

Oliphant: Isn't that right, Wayne?

Taylor: Henry talked to Sumner Welles without anybody else there, and after that meeting we got the impression - I think we (Taylor and Hanes) were both there at the

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same time - that they didn't want to do it direct with the Chinese Government, but wanted to do it with an American Corporation.

Oliphant: And that that would satisfy them.

Taylor: Well, that's ....

Hanes: But the - here's one ...

Taylor: ... one of those second-hand conversations.

Hanes: Henry called me on the phone - I got a note on my desk that I wrote down at the time, because he said, "The State Department will have nothing to say about it and will be delighted for us to go ahead, provided this money is loaned not to the Chinese Government but to an American corporation; for instance," he said, "the Archer, Daniels, Midland Company." Now, that gave me the impression that the State Department was saying, "If you lend to an American manufacturer, that's all right, but if you lend to the Chinese Government, we'll have something to say about it."

I think the best thing for us to do is to call up Sumner Welles, if you think it advisable, and just let's get that straight before we proceed any further with the American manufacturer - let's get straight what the State Department is saying. Do you think that's wise or advisable?

Oliphant: I think, since he mentioned his plans A and B - I think the thing to do is draft it as Plan A and draft it as Plan B, and one involving financing of Chinco and the other involving financing through Archer, Daniels. That's the way I'd do it.

Hanes: Of course, we've got two American manufacturers with large investments over there now, and ....

Oliphant: Well now, they're the middlemen, aren't they?

Hanes: Yes, they're the middlemen.

Oliphant: And they're to be taken care of on a commission basis.

Hanes: But my thought was this. What we're trying to do is to

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do this thing without - with the least upset to the existing machinery. Now you've got two American manufacturers who have got existing machinery in China.

Oliphant: American manufacturers?

Hanes: I mean American importers.

Oliphant: Middlemen.

Hanes: Yes, middlemen, who have got machinery in China for the purpose of bringing this tung oil in.

Oliphant: And with whom we have conferred.

Hanes: Yes.

Lochhead: Now the thing is, will they be in on it?

Oliphant: Now, somebody's got to raise the question with them whether or not they'll be satisfied with the commission arrangement. From the way they've talked, I think they would be, because they seemed to think of it as sort of an unprofitable business.

Hanes: I think they'd be delighted, because the way it is now - they told us they had from \$750,000 to \$1,500,000 invested in that thing all the time and it's a grave risk, because the stuff went down to four and a half cents a pound from thirty-five.

Lochhead: (Asks Oliphant a question in undertone)

Oliphant: I imagine they are. It's the old story of getting stuff out of Hankow.

Well, John, why haven't you got a little leeway on that commission business? That is, couldn't they be kept happy by sweetening that a little bit?

Hanes: By what?

Oliphant: Sweetening it a little bit.

Hanes: I think so. I think they would be happy.

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- Oliphant: They said the critical point of the price of tung oil was 12 cents c.i.f. (cost-insurance-freight) New York, and Chen said 11½ cents, didn't he, one day?
- Hanes: He said 11 cents.
- Oliphant: 11 or 11½.
- Lockhead: Then he also had a sliding proposition: 11 cents or 11½ if things would be taken down the normal way; if additional expenses - if taken down by truck, you might have to add the additional expenses to the base price of 11 cents. And that brings up the question of whether or not, if that brings it up to 15 - whether the people are ...
- Hanes: Can't sell it above 12, they say.
- Oliphant: The volume of consumption begins to decrease above 12. It doesn't disappear until you get pretty high, but the volume decreases above 12.
- Lockhead: Personally, I think the question is not going to be whether you get the price, but whether or not you're going to get the tung oil. It's one thing to guarantee a price, but can you guarantee the tung oil?
- Oliphant: You can guarantee that they'll get all that's coming out, to the exclusion of London and - and Germany, see? Well, that must be a tremendous advantage to the American manufacturers, to realize that they have the first call on any tung oil that does get out.
- Lockhead: I think that's going to be more important than price.
- Oliphant: Well, you remember the Secretary spoke with some vigor on the question of not hurting the people whom we called down here to confer, and I think that matter of commission has got to be discussed.
- Haylor: Well, you're not going to be able to protect them very much over in China, but after all, they're the same people, whether they're using some of the boys out there, in their organization out there, or whether they're using their organization here. I mean that's the major portion of their operation here anyhow - is on this side. But as I understand this plan, why,

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there's no place where they can get in over on the other side. I don't see how they can be utilized.

Oliphant: Well, they have facilities for gathering the stuff. The stuff is grown, produced in little bits of handfuls all over millions of ...

Taylor: Well, you've got a Government monopoly created over on the other side. How the hell do they get in on it?

Lockhead: The Government will probably absorb their organization over there. That's the way it will work out.

Taylor: They don't get any oil.

Lockhead: As you say, for their investment that they have over there and their facilities over there, probably the Chinese monopoly will either absorb that or take it over, pay them for it.

Taylor: But they're the same people, after all, and if they get in on something on this end, why, you don't have to worry about them very much. I don't see how you're going to work out using their facilities on the other end.

Hanes: I think so long as we do everything in our power to see that this Chinese company uses the facilities which are available over there and not set up - in other words, not set up competitive facilities for our American manufacturers - that seems to be important; we don't want to destroy our American investment in China if we can help it. want to help save it if we can.

Taylor: I don't - still don't see how that will be practical - possible to do it if you create a Government monopoly over there to do it.

(Foley brings in Mr. Morris;  
he is introduced)

Oliphant: Sit down, Lawrence.

Hanes: You could protect your American manufacturer by this Chinese company making its contract and doing its business through those two people who have facilities. There may be other people that have facilities there



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besides these two. Maybe W. R. Grace has some facilities there also. I know that Spencer, Kellogg and Archer, Daniels, Midland - I know they have some facilities there. They've got quite an extensive investment. And it was Henry's idea that we should do - not do anything to damage ....

Oliphant: ...them.

Hanes: ...those people in any way. And they're trying to help us get the thing solved.

Oliphant: This would just involve shifting their operations from an uncertain profit basis to a certain commission basis.

Hanes: That's right.

Oliphant: And performing the same fiscal operations they're performing now, working it into this Chinese monopoly thing. I've got my fingers crossed about their attempting a Government monopoly. You'll find the individual fellow who owns the individual tree won't give up that tung oil unless he's paid for it.

Taylor: Sure he gets paid for it.

Oliphant: Ordinary case of the Chinese going out and buying that tung oil. If you buy it from the local Chinese, you've got to buy it from these local outfits of Archer, Daniels and the rest of them.

Taylor: I don't think you'll find that Archer, Daniels has any investment in trees or oil over there. They're just ordinary middlemen - commission house over there that has a staff over there that buys and ships tung oil.

Oliphant: Well, they probably have some stuff in storage.

Hanes: Storage facilities and certain transportation facilities. How deep that goes I don't know. They didn't tell us. Just said, "We've got so much investment." I've forgotten what they had said. Seems they said around a million dollars investment.

Oliphant: Got some storage comprised in various sizes - storage points of various size.

Taylor: If their storage happens to be at any of the places

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where this is going to come out, which is unlikely, why, then you can rent their storage from them - the Government can. But I don't see how the hell they get in on any other basis over there. Now, over here - that's something else again.

Hanes: Well, I think we'd have to - we'd have to explore that with them to find out just what those facilities were. We didn't go into it very deeply with them, because we weren't thinking then in terms of doing it the way we are now.

Foley: Lawrence, we're talking about financing Universal Trading Corporation as one alternative, or the importers of - I mean the regular importers of tung oil....

Oliphant: The users of tung oil.

Foley: .... on the other hand.

Oliphant: At the moment the importers are middlemen, aren't they?

Foley: Yes.

Oliphant: Well, that, then, is the general plan: that the Chinese Government, getting this oil anyway they want to get it, whether by seizure or purchase or what not, purport to sell, or sell, the oil to the Universal Trading Company, right? And then that trading company, in turn, makes contracts with the users of the tung oil, the manufacturers, in this country, apportioning the oil on a basis of their previous year's supply. And I understand we're to get - they agree to send all the oil here, is that right?

Hanes: That's right.

Morris: Mr. Oliphant, is one of the purposes that of building up inventories in this country to a sufficient extent to protect the American market and insure their supply?

Hanes: No, I think it wasn't with an idea of building up inventories. It was the idea of taking this oil as it comes out of China and the Chinese Government contracting to deliver all the available tung oil to an American - to American manufacturers. If the American

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manufacturers can't consume it, there is no obligation on the part of the American manufacturer to buy it.

Oliphant: Now, what's the provision he had with reference to sale abroad by the Universal Corporation of any excess over American requirements?

Foley: Well ....

Oliphant: That's provided for in the plan, isn't it?

Foley: Yes, I think the plan said anything over and above 75,000 tons could be sold anywhere the corporation wanted to sell it.

Oliphant: And it could be sold regardless of where the tung oil was.

Foley: And regardless of where the tung oil was.

Oliphant: Could be shipped to London directly from China.

Well then, the final item in the program was that the present machinery of distribution operated by the private middlemen would continue to be used, but used on a commission basis as opposed to a profit basis. That's the plan we were working on.

Morris: That is, the Universal Trading Corporation would sell on a commission to ...

Oliphant: No, the Universal Trading Corporation would pay these middlemen who are now physically handling the stuff a commission for what they're doing. What they are now doing - what these middlemen now do - they're taking flyers in tung oil. They go out and buy the stuff, you see, and take a chance on selling it to the American user and hence they're getting a profit for that risk-taking.

An alternative would have been, wouldn't it, to give the middlemen a monopoly in the thing with an opportunity to make a profit on some small users and freeze out others too. Is that about it, Ed?

Foley: I think so.

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- Morris: One of the objectives of the plan - is it not to attempt to increase the sale of tung oil in the United States or to insure a steady supply?
- Oliphant: Well, the latter, yes.
- Morris: The fact that if it's needed they'd be sure of having their supply and then make commitments ahead of time to manufacture products - manufactures which use tung oil.
- Oliphant: No word from White, huh?
- McConnell: (Nods no)
- Oliphant: We'll have to appoint an investigating committee to look for him.
- Wess: Broadcast on short wave. Probably could tune in.
- Oliphant: Well now, Lawrence will be here today, Johnny, to work with you on this thing. Ed's available.
- Wess: All right.
- Boley: We'll probably want to get hold of the Chinese and talk to them. They don't know what Lawrence has done. Lawrence hasn't been able to contact them.
- Wess: I haven't yet got an answer to this other question we asked, as to whether or not before we - no use of drawing up the plan if this plan is going to run afoul of the State Department right away. Now, do you - is it all right if I go to see Sumner Welles and ask Sumner Welles the simple question, would the State Department have any objection to the Export-Import Bank making a loan direct to the Universal Corporation?
- Oliphant: If I were handling that, I would avoid that. I would avoid letting the State Department take a position on it at this time. Leave that for the Secretary to handle personally with the President or Secretary of State or Welles, as he thought best. I would suggest for today that we draw the plan in two forms, one which we know satisfies Sumner Welles, and the other which we prefer and which would require a little discussion. So I'd draw Plan A, financing the ...

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Hanes: The Universal Company.

Oliphant: ... Universal Company, and Plan B, financing the American users.

Taylor: I'd do both of them and have them very specific before I'd ask the State Department about an opinion on it, because if you don't have it specific, well, they'll say, "Well, let's see you carry it a little further."

Oliphant: Well, is that all the milk there is in that coconut?

Hanes: I guess that's all.

Taylor: John, isn't this really what you want? I've written them down here.

Seems to me you want three contracts. First you want the contract between whoever it is in China that's going to ...

Foley: The Republic.

Hanes: Chinese Government.

Taylor: Well, all right - that's a big order. I mean who the hell is the Chinese Government? Is it a - is this some new monopoly of the Minister of Transportation, or who is it?

Lochhead: They'll make that to our order over there.

Taylor: But it's important.

Lochhead: Mr. Kung.

Taylor: Personally.

Hanes: He's the Chinese financial government. He's the one we think about as ....

Lochhead: That will be the source.

Taylor: Be very specific as to who the contractor on the other end is. And that is between the Minister of Transportation, guaranteed by the - whoever it may be - the King and the royal family and the girls.....

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Lochhead: And the Madame.

Taylor: ... with Universal. And that will be to deliver X amount of oil over a wide period, and should also specify what Universal is going to pay for it, and how.

Then you have a contract between Universal and American jobbers on this end.

Whiphant: On a commission basis.

Taylor: Well, that's your ....

Morris: Would that be a series of individual contracts, or one contract with a syndicate of all the American companies?

Taylor: Well, if you have one contract, you can decide after you have it whether it's going to be with the - I think you assume that it's with an individual; then you can have them grouped together, if you want to, on the other hand. But I think your contract will be the same in any case, won't it?

Whiphant: No. Not one contract. Sherman Act.

Morris: You can't do it on one contract.

Taylor: This will be your model contract.

Murray: With individual jobbers.

Taylor: With an individual jobber.

Whiphant: To supply jobbing services on a commission basis.

Taylor: Yes.

Whiphant: But the apportionment of the oil will be made by Universal to the users on the basis of their - of their previous use.

Lochhead: That's the users, not the middlemen. The users don't get together.

Morris: You mean importers, not the users.

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- Oliphant: I mean the users; I mean the manufacturers.
- Lochhead: Sherwin-Williams, for instance.
- Oliphant: Let me make this clear.
- Foley: He gets his commission by rendering middleman services and delivering it.
- Oliphant: I think the law there is simple. Let's get it clear now. If we're the tung oil users, the manufacturers in this country, and we all get together and say, "Now let's all go and buy our tung oil from Universal at 12 cents a pound," you're in trouble with the Sherman Act, see? That's a conspiracy to fix a price. Now, if, on the other hand, I am the International - or, I mean the Universal, and I have the tung oil, and I say, "Now to all comers, I'm going to let them have it at so much on the basis of their previous use," it involves no confederation on the part of the users, you see. I'm fixing the price because I happen to have it, that's all, and there's no violation of law.
- Hanes: Uh-huh. Now, to ....
- Taylor: That has to be - you have to express that percentage of previous use and so on. But that's going to be - it's going to be, and, I would think, appear in your contract with your jobbers, because they're undertaking to handle this stuff according to a plan which you lay down. It isn't going to be with the individual American user.
- Hanes: The practical way to do this thing, if you could do it without interference with the anti-trust law, would be for the Universal Company to engage the services of the American importers - say, call them Archer, Daniels, Midland here for a moment - to engage their services at, we'll say, a half a cent a pound commission for distributing this oil to the consumers; because so many of these consumers are fellows that buy in quantities of one and two hundred pounds, and they can't go to the Universal Company and make a contract for the delivery and figure out what percentage two hundred pounds is going to be over a period of years. They don't know what their percentage is going to be. But if you could make a contract with X - Archer, Daniels,

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Middlemen, call them - for the distribution of this oil, apportioning among those distributors the total amount of the supply that we've got on hand in relation to the amount that they have themselves imported in the preceding year or preceding five years, or whatever it is, then you've got a practical way for the distribution amongst the manufacturers and consumers - the ultimate consumers of the oil.

Now, I don't know whether that can be done without - I don't see where we're doing any different if we trade with the middlemen and say, "You fellows imported 80 percent of the oil last year. We're going to give you 80 percent of whatever we get. If we get a hundred pounds you're going to get 80 of it, and you can distribute it to your customers at any price you can get for it. We're not - we set the price to you and you set the price." All we can say to them - "You can pass this oil on to the consumers at a price not in excess of ...."

Bochhead: You'd have to do that. Otherwise, you're giving them the monopoly.

Taylor: Yes, it seems to me you have to give them a handling charge basis and they deliver according to your instructions, according to the previous percentage. If you simply sell it to them direct, why, you're going to run into some trouble there. Then you do create your - what amounts to a monopoly, and so forth, for those, let's say, two or three jobbers, don't you, Herman?

Wright: I was trying to figure out whether or not there was some way to step back one notch and deal with the jobber.

Taylor: Well, this thing - won't this thing that I'm describing just about do that? You make a contract with your jobber to deliver according to a certain schedule, and you pay him for that.

Wright: All you've got to do is to avoid concerted or group action on the part of either the American users or the American importers.

Taylor: Well, won't that do it?



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- Hanes: Is it group action if we call in three importers who import 80 percent of the entire amount and say to them, "We're going to fix it so you can make a contract as individuals, not as a group - but make a contract as individuals with this Chinese company for - your share was 20 percent, your share was 30 percent, your share was 30 percent" - so forth.
- Oliphant: I'm a little afraid of it.
- Taylor: That's what Herman's worrying about.
- Oliphant: You've got - it violates the Sherman Act either to get together and fix price or to get together and apportion supplies. One is as bad as the other - the old division of territory.
- Taylor: Can't you do it ....
- Morris: Who does the apportioning: isn't that the fundamental point? If whoever does the apportioning says, "You want 30 percent, but you can't have it; but I'll give you 20 percent. I'll give so much to you" - the Universal is doing the apportioning, not the buyer.
- Taylor: Seems to me Universal has to do the apportioning, and you hire these other guys simply to handle it for you.
- Oliphant: If Universal does the apportioning - suppose we don't don't confer with anybody any more - we've got to be careful not to confer with them any more - suppose we don't confer any more and Universal does the apportionment. Is there any reason why they shouldn't apportion it among the importers and let the importers handle it on a profit basis? I think that's Jones's idea, isn't it, John?
- Hanes: Yes. Of course, if we make a contract - if we just lend this money to the Universal Company and say, "In return for this we demand a contract with the Chinese Government, whoever that might be, for the delivery of all Chinese tung oil to this shore; by the time it gets here, then all comers may get such portion of this oil as you want to sell them, that's up to you entirely" - that would be the situation if you had the Chinese company functioning as a distributor in this country. Then everybody would get it. If we could set

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the price all right, just make a maximum price - but everybody would get oil as they needed it and when they needed it. But that, in my opinion, is doing a real damage to the fellow who's now got an investment in there and is doing a little of the work toward importing the oil to this country.

Taylor: Well, unless you pay them as a handling charge, which as I understand is what Herman's talking about.

Hanes: But that again - I don't see how you're going to make this deal without getting these fellows and talking to them, and when you get them and talk to them then you're ganging up.

Taylor: They've got to be parties to a contract and I don't see how you can do it without it.

Oliphant: Or separately parties to a series of contracts.

Taylor: But one of them has to be a - let's say one of them has to be party to a contract to do certain things.

Oliphant: Taking him as an example.

Taylor: Yes. I think that contract is going to be to deliver on "your" order to some paint manufacturer - I mean "your" order being Universal's order. Because if you do it the other way, why, you run up against this control of a supply and having them feed it out and so on.

Morris: Are there a few big handlers now that take most of the market or the whole market?

Hanes: Yes, there are three big ones. That's the - W. R. Grace is the smallest of the three big ones. Archer, Daniels, Midland is the largest. Spencer-Kellogg is next.

Oliphant: Are there lots of little middlemen?

Hanes: Yes, there are lots of little middlemen. The biggest of the little middlemen is a man by the name of Jackson. His representative was down here. We talked with him same time we talked with the other people. Now, my understanding is that the four people we talked to have

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approximately between 70 and 80 percent of the supply that's in this country at the present moment, which amounts to about 18,000 pounds.

- Taylor: Now, your third contract is one between the - either the Export-Import Bank or the R.F.C., and Universal. Now, if you want a fourth contract, see, as an alternative, between the Government credit agency and either your middleman or your consumer, why, try to work that one out.
- Morris: I don't believe Universal could get started a distributing organization of its own. Couldn't possibly do it.
- Hanes: No, and they don't want to do it. My understanding is that they don't want to do it. Want to have it done by the regular American distributors.
- Lochhead: Want to have it done by the regular middlemen; just act as a go-between.

## PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: October 19, 4 p.m.

No.: 1784.

FROM COCHRAN

At 12:00 o'clock noon I visited the Bank of France.

The French stabilization fund had acquired \$118,000 on a thin market by that time. The French stabilization fund had gained \$221,000 on Monday, and on Tuesday, \$223,000. It has not bought any dollars this week. As it is not known what political and financial measures France may take during the next 3 weeks, the franc stable "in suspense"—even given some benefit of doubt. Upon my mentioning the rumors that the Government might call on Baudoin or Rist for expert aid my friend pointed out that these names were the ones usually suggested when financial confidence and recovery were being sought by a Government. The fact that Baudoin is already successful as an independent exchange operator has heightened the skepticism of the majority of my friends as to Baudoin's going into the Government now.

When I inquired of my friend at the bank as to the best means of assistance for French aviation, he stated that it would be most helpful if Blum's admirers would persuade him to influence workmen to perform their patriotic duty in the aeronautic factories which already exist in France and which employ them.

The

- 2 -

The British stabilization fund had by twelve noon purchased a half million dollars. The fund found however that the market was so thin and nervous that the trend would have been reversed if there were much official effort at buying dollars. There is fear among Bank of England traders that the present lack of faith in currencies may give rise to new hoarding of gold; this sentiment was expressed also by Cobbold when I saw him at Basel.

There is considerable attention in the French press to stories of German trade credits to Poland and Turkey. There are also reports on the prospects for German trade penetration following the visit to the Near East of Minister Funk. There is a dawning realization on the part of France of the stiff competition that will now be waged for trade in this hemisphere by Great Britain and Germany, in spite of the liberal trade policies advocated at Geneva by the French delegates. The French appear quite realistic in their present efforts to hold their own; this is shown by the arrangements announced in the press of a barter of French wheat for sulphur from Italy, and a large sale of subsidized wheat to a British concern; the National Wheat Office took care of both deals.

There is a revival of the AGENCE ECONOMIQUE'S periodic arguments in favor of abrogation of the Johnson Act, settlement of the war debt question, and extension of loans between countries belonging to the Tripartite.

Today

- 3 -

Today 450,000 florins were <sup>bought</sup> ~~made~~ by Paris-American Bank, for the French control. It is presumed this purchase was made to pay interest due on the twentieth of October on the Dutch banking credit.

END MESSAGE.

WILSON.

RECEIVED  
OCT 20 1918  
THE GREAT SEAL  
U.S. DEPARTMENT OF STATE  
WASHINGTON, D.C.

EA:LWW

REB

GRAY

London

Dated October 19, 1938

Rec'd 4:30 p. m.

Secretary of State,  
Washington.

1211, October 19, 6 p. m.

FOR TREASURY FROM BUTTERWORTH:

The dollar opened at 4.77 offered and after moving to 4.76 5/8 returned to 4.77 1/4 at gold fixing. 139 bars were dealt in at 145 shillings 8 and one-half pence, a half penny premium. After gold fixing the rate remained at 4.77 5/8 until New York came in a strong buyer of dollars. The rate moved to 4.77 1/8 but later returned to one-half on offerings from Paris. The volume of trading has not been large and dealers are puzzled as to whether the British authorities have been operating today but inasmuch as the two steady sellers of dollars were the Bank of Scotland and Hambro's it is more than likely that the British authorities have intervened through the above as agents. Although the pound has not been under strong selling pressure since the end of last week and has somewhat appreciated in terms of dollars there has been no corresponding return of confidence

REB

2-#1211, From London, Oct. 19, 6p.m.

confidence in sterling in the city. However, some bear speculators are beginning to be nervous.

The franc was again somewhat bid.

KENNELY

NPL

EMB

RECEIVED  
OCT 21 1963  
FEDERAL BUREAU OF INVESTIGATION  
U. S. DEPARTMENT OF JUSTICE



RAW

A portion of this telegram must be closely paraphrased before being communicated to anyone. (B)

Berlin (part air)

Dated October 20, 1938

Rec'd 9:30 a.m., 21st.

Secretary of State,

Washington.

564, October 20, 9 p.m.

(GRAY) 25. FOR TREASURY FROM HEATH.

Under such headlines as "progressive reduction of Reichsbank credits" the German controlled press is hailing as an achievement the considerable reduction in credits and currency circulation shown in the mid October statement of the Reichsbank.

Roughly 1,217 million reichsmarks or 73% of the huge September increase of Reichsbank credits have been repaid during the first half of the month. This is about the normal percentage rate of repayment however. At mid October 1937 71.4% of fresh credits of the previous month were repaid. The Reichsbank bill holdings on October 15 were 6,986 million reichsmarks a decrease of 350,000,000 reichsmarks from October 8. In mid October 1937 bill holdings were 5,000 million reichsmarks.

Total currency in circulation decreased by 888 million reichsmarks to the figure of 9,266 million reichsmarks on October 15 which is still 331 million reichsmarks over the circulation at the end of August and 558 million reichsmarks

OVER

-2- 564, October 20, 9 p.m., from Berlin.

over the mid September circulation figure. In short the Reichsbank has not yet deflated the large currency and credit increase of the second half of September.

September foreign trade figures for greater Germany (including Austria) show a passive balance of 50.8 million reichsmarks as compared with a passive balance of 64.5 million reichsmarks in August. In the trade of Germany proper (not including Austria) there has accumulated during the first nine months of the year a passive merchandise trade balance of 257 million reichsmarks as compared with an export surplus of 311 million reichsmarks for the first three quarters of 1937.

Merchandise exports from Germany proper for the first nine months total 3,857 million reichsmarks <sup>a decrease</sup> of 420 million reichsmarks or around 10% from the figure for the first nine months of 1937. Imports totaling 4,021 million reichsmarks showed a slight increase over imports for the first three quarters of 1937 which were valued at 3,970 million reichsmarks. It must be said that given the depression in important foreign markets Germany has fairly well succeeded in maintaining its foreign trade. An excess of imports over exports can be maintained for a while with some countries as long as they are willing to accept blocked marks in payment.

The

- 3 -

The continued passive trade balance and decrease in exports are causing worry however as is evidenced (1) by Funk's recent letter to the Reich Economic Chamber in which he exhorted German manufacturers to fresh efforts for export trade and (2) the attempts of the German Government to persuade England to begin the negotiations for mutual tariff concessions called for by a clause in the Anglo-German agreement of last June. The British Government, according to British sources here, now is disinclined to enter into such negotiations until the political atmosphere is further clarified. Information comes from the same source that the British Government is completely aware that Germany had been enabled, through the relatively favorable trade and payment arrangements granted by England, to purchase raw materials not of English origin on the London market, which materials were used for military preparation and rearmament in Germany. These purchases would not have been possible had the trade agreement been a clearing agreement of the type of the Swiss arrangement, unless free exchange and gold reserves had been used by Germany.

In previous telegrams it has been noted that Germany's import surplus for the first seven months of this year was accompanied by net gold imports of 92.5 million reichsmarks.

-4- 564, October 20, 9 p.m., from Berlin.

reichsmarks. In the last two months, however, there has been a still larger outflow of gold so that for the first nine months exports of gold exceeded imports by 19.5 million reichsmarks. In September alone there was a net export of 91 million reichsmarks of gold. These statistics apply only to shipments from Germany proper.

I saw Brinkmann and Bergemann of the Economics Ministry today. The latter said that no progress had been made in the German-Czech negotiations for a new tariff and payment arrangements during the last ten days. Various small quotas had been discussed but he asserted that it could not yet be predicted what would be the ultimate tariff and payment arrangements between the two countries. (END GRAY)

WILSON

KLP

REB

GRAY

London

Dated October 20, 1938

Rec'd 3:25 p. m.

Secretary of State,  
Washington.

1219, October 20, 6 p. m.

FOR TREASURY FROM BUTTERWORTH:

The volume of trading in the dollar-sterling exchange has been larger today and apparently the continent attaches importance to rumors regarding Memel and Danzig. The dollar opened at 4.77 3/4 and quickly moved to 4.78 on offerings. It soon turned and slowly but surely moved to 4.75 1/2 with the British authorities checking the movement from time to time. Likewise gold fixing was larger, 397 bars at 145 shillings one-half pence, parity, of which 137 and the remainder supplied by the British fund. Most exchange dealers have been caught by the rapid turn and because the bidding for dollars has come in so much stronger than the offerings of recent days they are inclined to feel that this is the beginning of another buying wave.

The following excerpt from the city columns of today's TIMES may be of interest: "The market was inclined yesterday to be critical of the authorities for allowing the  
rate

REB

2-#1219, From London, Oct. 20, 6p.m.

rate to rise so sharply instead of replenishing their reserves. But there are naturally two considerations which have to be borne in mind. One is that there is a real tactical and psychological advantage in having the rate appreciably above its post Munich low point. The other is that the feelings of Washington which may have been a little ruffled at the landslide of a week ago can not at the present juncture be wholly ignored. It is still more than possible at the same time that the present policy will do most to bring about a more stable period in which some quiet replenishment of depleted gold reserves can be undertaken."

KENNEDY

CSB

## PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: October 20, 1938, 4 p.m.

NO.: 1789

FROM COCHRAN.

Last night I had a talk with the representative of the Bank of Italy, who expressed to me his keen interest in seeing Italy's relations with the British normalized at an early date. My friend emphasized the efforts which Italy had put forth to improve its relations with Hungary and Poland and thought the best way to check German trade penetration eastward would be for those three countries to work more closely together and to cooperate in this with Great Britain and with France if possible. Even though Italy realizes Germany's natural trade with the area under reference, she also has a normal claim to important commercial interests with this region and would be greatly disturbed to see such a thing develop as a German monopoly. My friends of the Bank of Italy are most anxious considering the relationship of the lira with the dollar as to how far the United States would be disposed to see the sterling weaken without taking action of a restraining or retaliatory nature. The opinion is held by the Bank of Italy representative in London that the pound will depreciate beyond 4.60 and possibly beyond 4.50. (END SECTION ONE)

PARAPHRASE.

SECTION TWO. Telegram No. 1789 of October 20, 1938, from Paris

A few days ago when I was in Basel some of my friends there were arguing that Germany's very obvious determination to expand her foreign trade may be one of the best reasons for and means of Germany returning to a monetary system which is more stable and more orthodox. In other words, Germany will see the advantage of adopting a monetary unit which is more capable of fitting normally into the foreign exchange system of the world in order to enlarge German foreign commerce above the restricted and diminishing level which is involved in clearing agreements and barter arrangements. There is common agreement among my friends that it will not be possible for Germany simply to abandon exchange control and other obstacles to foreign trade immediately, and to adopt at the same time a new monetary system. It is their belief that if the export trade of Germany is extended, it will tend to relieve the situation which makes imperative foreign exchange control and related economic measures. Some halt in armaments is necessarily anticipated.

END SECTION TWO.

WILSON.

EA:LWW



PARAPHRASE  
SECTION THREE. Telegram No. 1789 of Oct. 20, 1938 from Paris

It is my friends' belief that during the next few weeks and months there will be many uncertainties, and that perhaps in various countries there will occur difficult negotiations incidental to political and financial crises. When these difficulties are gone, some of them think, there may emerge an era of peace, conceivably including at least moderation in arming, and that in Europe there will be a return to comparative prosperity. It is likely that, with such hopes in mind, the coming months may witness a revival of those measures by which European countries increase and consolidate their international influence, such as loans and direct investments abroad, negotiation of trade treaties, despatching of commissions and envoys on financial and commercial matters, and so on.

END SECTION THREE.

PARAPHRASE.  
SECTION FOUR. Telegram No. 1789 of October 20, 1938, from  
Paris.

That the British and French should devote particular attention to their trade with the Germans is entirely reasonable, since Germany is after all a much larger potential customer than many of the Near Eastern countries taken together. It is logical that those countries which now or in the near future supply large consumers like Germany and Italy with necessary raw materials - by clearings, credits or barter - may be expected to retain certain preferential advantages when Germany and Italy have recovered sufficiently to get their supplies on lines of trade which are more normal.

END SECTION FOUR.

WILSON.

EA:LWW

## PARAPHRASE

SECTION FIVE. Telegram No. 1789 of Oct. 20, 1938 from Paris

The competing European countries will of course be interested in seeing the extent to which the United States may try to retain or enlarge its trade with the countries in the Eastern part of Europe, and in the parts of the Near East which are most vitally concerned in the new struggle for supremacy in trade, as well as with Germany and Italy, the two countries whose trade relations - until their new economic systems led to new trade practices - were always very important to the United States. The question is whether the United States will push its program of reciprocal trade agreements or whether the policies of the Johnson Act and the Securities and Exchange Commission will be relaxed, as they stand in the way of lending to the most potential European borrowers despite our large accumulation of wealth and their poverty. Other questions are whether the United States would revise its national trade program in order to give consideration to those countries which for the time being are not in a position to meet all the requirements of its system, or whether the United States will be satisfied with concentrating on the Latin American countries, which are sparsely settled and slow in paying.

WILSON.

REB

GRAY

Paris

Dated October 20, 1938

Rec'd 2:30 p. m.

Secretary of State,  
Washington.

1789, October 20, 4 p. m. (SECTION SIX)

A special article reviewing Britain's foreign trade policy in today's FINANCIAL TIMES concluded:

"Needless to say the entire policy of reciprocity, subsidies and tariff bargaining is in general repugnant to the liberal economic traditions upon which British trade has been built. Nevertheless, circumstances are now exceptional and international trade will not revive of its own accord. The greater necessity, then, is to secure for British exports a more reasonable share of the world's markets by expedients which shall be short termed without being short sighted."

An editorial on "Dr. Funk's progress" appearing in today's LONDON TIMES concludes: "perhaps the chief lesson for this country is that it might be well for us to review very carefully our own traditional methods and to seeing whether, without sacrificing anything of value,

WE

REB

2-#1789, From Paris, Oct. 20, 4p.m.  
(Sec. Six)

WE can modify them in a way which will enable us to compete more effectively with the new methods of the totalitarians."

Bank of France statement as of October 13 showed discounts down one billion four hundred and sixteen million francs, circulation down four billion eight hundred seventy-three million and advances to state reduced by two billion, leaving coverage 40.41 versus 39.30. My friend at the Bank of France told me the repayment by the Treasury had resulted from investment by public of dehoarded funds into Treasury bills.

In spite of above-mentioned favorable statement franc today weakened and French stabilization fund yielded sterling around 178.75. Sterling in turn weakened against the dollar.

(END OF MESSAGE)

WILSON

WVC

CSB

## PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Berlin, Germany (part air)

DATE: October 20, 1938, 8 p.m.

NO.: 563

Funk's Balkan trip continues to be the subject of extensive comment in the German press which is, however, for the most part of a general nature emphasizing the economic benefits to be derived from the formation of a Balkan "axis" consisting of Yugoslavia, Bulgaria and Turkey which would reach from the German frontier to the Black Sea. The most concrete result of the trip was the announcement of a credit to Turkey of 150 million marks presumably outside of the existing clearing to be utilized for the purchase of German railroad and bridge material, machinery and chemical products. This is no doubt intended to offset the recent British credit of 16 million pounds and is supplemented by assurances of a large permanent market for Turkish agricultural products. As to Bulgaria and Yugoslavia great stress was laid by Funk upon the German capacity to import large amounts of foodstuffs and raw materials at stable prices under long term agreements.

Yesterday Funk sent a letter to the Reich Economic

Chamber

- 2 -

Chamber directing German industry to give greater attention to export business despite the large demands of the domestic market and stating that neglect of exports must be considered as a "serious breach of duty" and concluding with the threat that "steps will be taken against firms which do not sufficiently fulfill their obligations to promote exports". This followed closely upon the publication of the September foreign trade figures which recorded another unfavorable balance for the month.

On October 18 it was announced that a credit of 60 million marks had been granted to Poland for the purchase of German industrial products and to be liquidated through German purchases of wood and agricultural products, particularly grain. This is to be additional to the trade carried on under the present German-Polish clearing.

Today's press reprints excerpts of an article published in the WASHINGTON POST this week relative to German trade with southeast Europe and emphasizes how German projects in this field will lead to an expanded world trade and thereby contribute to constructive political action.

I had a talk with Bergmann of the Ministry of Economics today. He said that while the export credit granted to Turkey was helpful, it was not of great importance, and that he himself was doubtful whether the Turks would be able

to

- 3 -

to ~~me~~ take up the whole credit, and that if Turkey should order 150 million marks worth of production goods in addition to its present imports from Germany, it would be strung out over two or three years. In Bergmann's opinion the credit in the amount of 60 million marks just granted to Poland would be altogether utilized, since modern equipment for its steel mills and smelting plants will take up half of the credit. He expressed doubt whether the Balkan countries, on the import side, could greatly increase their production of essential raw materials in which Germany was interested. He believes that an enlarged agreement with the British and a trade Agreement with our country would be the real solution of German trade difficulties.

You are requested to inform Treasury of the appropriate portions of this telegram.

WILSON.

EA:LWW



## GROUP MEETING

October 20, 1938.  
9:30 A. M.

Present: Mr. Oliphant  
Mr. Gaston  
Mr. Haas  
Mr. Taylor  
Mr. Hanes  
Mr. Upham  
Mr. Gibbons  
Mr. White  
Mr. Lochhead  
Mr. Bell  
Mr. McReynolds  
Mrs. Klotz

Bell: He (Mr. Aubrey Williams) said he'd come; I don't know whether he meant ....

H.M.Jr: Who spoke to him?

Bell: I did; I said you wanted to see him and Hopkins both. Did you tell Kieley to mention it?

H.M.Jr: Kieley just had a message from Aubrey Williams.  
(Telephone) Hello. Hello. Does she know she's in staff meeting? Wait a minute, I'll let her talk to you. All right.

(Mrs. Klotz takes telephone call in her office.)  
And come back in.

Klotz: Yes sir.

H.M.Jr: (To Mr. Gaston) Hello. Hello, Johnny.

Hanes: (Coming in) Good morning.

H.M.Jr: (To Mr. Kieley) What was the message from Mr. Aubrey Williams?

Kieley: That he hadn't heard any word from Hopkins.

H.M.Jr: All right.

- Bell: He would be willing to come, probably, if you wanted to see him.
- H.M.Jr: Well, there's no use; Hopkins spent the night with me, so I know what's on his mind.
- Bell: Yeah. How about the meeting at two fifteen?
- H.M.Jr: That's on.
- Bell: Still on?
- H.M.Jr: That's on, definitely. You're coming to that, and Taylor's coming to that, and I want Hanes, and Haas, please.
- Mac?
- McReynolds: You remember that musical organization over in Internal Revenue that Mrs. Anderson came to see you about?
- H.M.Jr: Yes, what about it?
- McReynolds: Well, I am giving permission to her, if you have no objection, to have notices posted around, inviting voluntary contributions to their organization. They have no income except what they provide themselves. I see no objection to doing that because it is a musical organization of employees of the Department. I told them they couldn't send petitions around for it, trying to get donations, but they could post on the bulletin boards, notice that permission was granted for voluntary contributions to be made.
- H.M.Jr: O. K.
- McReynolds: You gave me, or sent in to me, last week before you left, a note from Mr. Roosevelt ... (speaking low). I don't want to hold it any longer - about a chemist ..... (low) He has no Civil Service status; all the jobs are Civil Service; the only way he could get it would be by Executive Order.
- H.M.Jr: No, I don't want to do that. Write a letter, and I'll sign it.

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McReynolds: All right; that's all I've got.

H.M.Jr: Dan?

Bell: I wonder if it isn't about time we began to study legislation in connection with the public debt - the total amount that can be issued. Last year we got forty-five billion dollars limitation, and thirty billion dollars on bonds. At the end of this fiscal year that will be pretty well exhausted, or at least it will be so low we won't have the flexibility that we need.

H.M.Jr: All right. You might mention that at the two fifteen meeting. Sure. What?

Bell: All right.

H.M.Jr: You know I am going to call on you this afternoon to tell them what - just what we told the President, I mean, as we made it to him a week ago Monday.

Bell: All right.

H.M.Jr: What?

Bell: All right.

H.M.Jr: See, and I thought if Haas would have some of those charts showing the picture on national income, the ones that were National Income, Federal Reserve Index, and the index for prices, you know.

Haas: Yeah; all right.

H.M.Jr: And let them take a look at those.

Haas: That is all you want?

H.M.Jr: That, and plus what this year's thing is running - the bubble chart.

Haas: The bubbles.

H.M.Jr: The bubbles, and also the one showing whether - over and under - which groups.

- 4 -

Haas: Uh huh.

H.M.Jr: You know the one I mean?

Haas: I know the one. I have some others in the process.

H.M.Jr: I think you'd better be there, Mac, too today, because that is a question I want .....

McReynolds: Yes.

H.M.Jr: Well, it's a question, I think I told you people, which I told the President that I was inviting these people on a sort of trial basis, and the President said, "No, it's not a trial basis; they can have a season's pass, which is not renewable, and we'll see how it goes." He said, "We'll invite them to sit in once," but he didn't seem to think it would fit into what he had in mind if he got his reorganization bill through, so Mac had better sit in on it. The eventual plan that he has in mind - the White House way it is laid out - he doesn't seem to think this is the answer, but he will go ahead with it for one year, for the one Budget.

Bell: (Nods "Yes.")

H.M.Jr: Something else, Dan?

Bell: That is all.

H.M.Jr: (Nods to Mr. Lochhead.)

Lochhead: Still the pressure on sterling seems to be building up a little bit - down to 4.76 now; it's too early to tell anything on this market.

H.M.Jr: While we're on this thing, tomorrow I've got a meeting at ten - got some people coming in on sterling. Archie, you be here, and White, and Taylor, will you please, and I wish that those who are working on foreign exchange; that means White and Archie, Taylor and Oliphant, will take this over. I am not going to mention the man's name, but he gave me this idea, and it's worth thinking about. He thinks that the British are going to hold the pound where it is until they get the British Trade Treaty signed, and then as soon as it is signed they will let it go, but they are

just going to do everything they can to hold it where it is, and as soon as it is signed to let it go. And then, he says, that once it is signed I will just have the devil's own time trying to get that little section ; that Mr. Hull and everybody in the country will be against me and I'll be standing by myself; therefore, he makes what I consider a brilliant suggestion, and that is that before the thing is com- -signed we put in a floor to that; let's say four and a half, that if the pound should go below four and a half or four sixty, whatever we decide, automatically the thing is cancelled. In other words, an automatic clause, rather than an optional one, so I won't have this big fight with Mr. Hull. I think it is a brilliant suggestion; it will be automatic. I am taking the brunt for cancelling the British Trade Treaty and everything that goes with it.

Oliphant: That's up the floor and the ceiling too, so it looks all right.

H.M.Jr: Let them put on the ceiling; you put on the floor. I think you'll have to move fairly fast. And I thought you men might be thinking about it, and I possibly might bring it up at ten o'clock tomorrow. See? And, incidentally, I am going to talk about financing Central and South America to you people. You (Mr. Oliphant) had better sit in on it too. I know the the propaganda machine, Mr. Hull hasn't put on this thing, and for me to go up against that ..... (Aside to Mrs. Klotz.)

I think it's - they will just hold it long enough and then he said they will take the shirts right off our backs. So will you people be thinking about it? Huh?

Oliphant: (Nods "Yes")

H.M.Jr: I think he's right. I mean, he's right if it does go down and if you have an automatic thing which, if it goes through four fifty, why, the trade treaty is automatically off.

Taylor: You remember they wanted to do that earlier, and we turned it down.

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- H.M.Jr: Are you sure?
- Taylor: Uh huh.
- H.M.Jr: The British, I thought -- no. Will you reexamine that; I think you're wrong.
- White: It's somewhat different.
- H.M.Jr: What they wanted was: Number One, we should not have a right to put an embargo on gold. That was one, number one. Number Two, they wanted us to define that thing; put it in other words.
- Taylor: They wanted to put in a ten per cent clause there.
- White: At which point it would not be subject to reexamination unless it went through.
- H.M.Jr: If you people would look at it for me, and I lay great stress on this thing, because I can see, and the source is so smart, that I think he knows what he's talking about.
- White: The objection was not to the idea, but to the figure they used, of ten per cent, either way.
- H.M.Jr: Yeah. Well, as this man said to me, he said, ..... (speaking low) ... and I said, "Well, it's all figured on four ninety;" he said, "Well, four eighty, maybe you could say, wouldn't hurt you much; maybe four seventy you would be able to get by, but you've got to make up your minds that at four sixty you will lose your shirts and want to stop at four fifty."
- I don't think I'll have very much trouble with the President because the President, I don't think, will want to go through that fight either. I think it is fine.
- Oliphant: I think so too.
- Taylor: They were the people who started talking about it.
- H.M.Jr: If you are right, Wayne, it will be very easy, but I think we ought to do something fairly quickly about it.

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Now, the other thing on the foreign matter - two things, Wayne, I'd like you to handle on a twenty-four hour basis over there; one is this question of this silver at Tientsin - the new one that just came in. (Looks through memo.) Here, this is it; it's the only one I've got; you don't mind giving it back to Mrs. Klotz afterward. And this is, I take it, from the State Department, from the General Consul at Shanghai.

Taylor: Archie had talked to .....

Lochhead: That is the Tientsin ....

(Mr. Taylor and Mr. Lochhead talking at same time.)

H.M.Jr: I want a written recommendation to me from the State Department. What do they advise me to do?

Taylor: (Nods "Yes.")

H.M.Jr: See, I want to know what do they advise me to do? I mean, this is - and I want it in writing. And the other thing I'd like also, if you don't mind, to come back to Mrs. Klotz. This thing bothers me very much, and I wish - this is from the Canopus at Hongkong, in which he says it looks as though the British had a secret understanding with the Japanese on the Kowloon-Canton railroad, and I'd like the State Department to follow it through in London and find out how much more there is to it. I think it is important enough that we ought to know.

And this one, Archie, from Campbell, also to go back, I can't answer it, and you can just tell Nicholson it's a very nice idea, but I can't do it. If the British have got an understanding with the Japanese, prior to their invasion, I think it is terrifically important to know it.

And, incidentally, the President has not seen that memorandum - the change of the Bilateral Treaty; I'd like to get hold of it to give it to him.

White: I have the cable; it's just a cable.

H.M.Jr: Whatever is in that cable.

White: I have it on my desk.

H.M.Jr: Give it to Mrs. Klotz before eleven; I want to send it up to the President. He hasn't seen it; he's very much interested.

Now, in strictest confidence, I'd like to read a letter which I delivered to the President night before last, so you people will know what I am thinking. White helped me write this, to the President. He read it very carefully; he seemed very much interested, and he kept it. I didn't know whether he'd keep it or not.

"Dear Mr. President." As I say, this is very confidential, but at least, you will know where I stand.

"Dear Mr. President:

"The events of the past weeks have brought home to all of us the increasing effectiveness of the forces of aggression. Since 1931 we have seen, succeeding each other with briefer and briefer intervals between, the fall of Manchuria and the invasion of China, the conquest of Ethiopia, fomented unrest in Latin America and in the Near East, armed intervention in Spain, the annexation of Austria, and the dismemberment of Czechoslovakia -- All in seven short years.

"Nor can we expect aggression to end there. Japan at first wanted only Manchuria; then North China; now she will not be content with less than the whole of China. Italy wanted only Ethiopia; now she wants control of North Africa. Germany wanted only equality in armaments, then the remilitarization of the Rhineland, then Austria, the Czechoslovakia, now colonies. The current claim of an aggressor power is always its last -- until the next one.

"So well have the aggressor nations mastered the tactics of aggression that a victory in one part of the world is followed by outbursts of aggression elsewhere. Germany's victory in Czechoslovakia is followed with indecent haste by Polish and Hungarian



demands. Japan, watching her opportunity, loses no time in attacking Canton, while in Palestine, Arab discontent is fomented to fever pitch.

"We should learn the lesson which the history of the last seven years has to teach us. Let us not repeat the short-sighted mistakes of Britain and France. The impact of the aggressor nations upon American life and American interests has so far, to be sure, been more insidious than overt but it will be too late if we wait until the effects are obvious. Who in France as late as 1930 would have dreamt that in less than a decade that great democratic nation was to become a second-rate power, shorn of influence in central Europe, dependent upon a grudging and demanding ally for security? Who would have expected that Great Britain's might would be challenged in the Mediterranean, that her economic interests would be brushed aside in China, and that the Premier of England would hurry to Hitler to plead that he be not too demanding or impatient, and to plead, moreover in humble tones lest the dictator take umbrage and demand more?

"Let us while we can peacefully do so try to check the aggressors. Let us not be placed in the position of having to compound with them. Let it not be necessary for the President of the United States to fly to Tokyo and in humble manner plead with the Mikado that he be content with half the Philippines rather than wage war for the whole. Such a possibility may seem ridiculous now, but no more ridiculous than Chamberlain's flight to Berlin would have seemed seven years ago.

"In March of this year, Winston Churchill called upon England to act, saying 'If we do not stand up to the dictators now, we shall only prepare the day when we shall have to stand up to them under far more adverse conditions. Two years ago it was safe, three years ago it was easy, and four years ago a mere dispatch might have rectified the position ... Now the victors are the vanquished, and those who threw down their arms in the field and sued for an armistice are striding on to world mastery.'"

That's the end of the quote.

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"The basis for the present humiliation of England was laid in 1931, when England failed to join the United States in disapproval of Japanese aggression in Manchuria. The basis of either humiliation or war for the United States is being laid today by a foreign policy that shuts its eyes to aggression and withholds economic support from those who resist.

"I know you are firmly convinced as I am firmly convinced that the forces of aggression must be stopped. By whom if not by us? I believe that we are the only country in the world now in a position to initiate effective steps to stop aggression by peaceful means. Once the United States takes the lead in developing an effective program, democratic forces in all countries -- even those now submerged in the aggressor nations -- will take heart. In England and in France groups within the government and without will be stimulated and encouraged to press for parallel action.

"To use our great financial strength to help safeguard future peace for the United States, and to make your 'Good Neighbor' policy really effective, we should introduce at once a program of peaceful action on two fronts -- in the Far East and in Latin America. In these two areas we can move most effectively and with the least complication.

"Two opportunities are now before us:

"1. The extension of credit to China. It is yet possible for such aid to be of decisive help. Sanguine as I desire to be, I am forced to the view that without substantial financial aid given promptly the Chinese resistance may soon disintegrate. By risking little more than the cost of one battleship we can give renewed vitality and effectiveness to the Chinese. We can do more than that. By our action we can further the struggle of democracy against aggression everywhere.

"I am pleading China's cause with a special urgency because you have on numerous occasions told me to proceed with proposals for assistance to China. All my efforts to secure immediate substantial aid for China have proved of no avail against the adamant foreign policy of doing nothing which could possibly

be objected to by an aggressor nation. I need not tell you that I respect the integrity and sincerity of those who hold the belief that a course of inaction is the right one, but the issues at stake go beyond any one of us and do not permit me to remain silent. What greater force for peace could there be than the emergence of a unified China?

"2. The extension of credit to Latin American countries. Our neighbors to the south are sorely in need of capital and commerce to enable them to develop their resources free from foreign intervention. Unless we assist them they will become a helpless field for political and economic exploitation by the aggressor nations. Already some inroads have been made in that direction. Now, after the Munich agreement, we may expect that Germany, Italy and Japan will become bolder and more effective in their attempts to establish areas of economic and political support to the south of us. We can stop that penetration by an intelligent use of a small proportion of our enormous gold and silver holdings.

"The measures we may adopt can be developed as the specific occasions requiring assistance may arise. We have several such occasions before us right now: Brazil, Cuba, Mexico, Peru. The details of the Assistance can be worked out in conjunction with the representatives of those governments, but it is first necessary that we accept in principle the need for positive action of this kind as a part of our 'Good Neighbor' policy.

"European events of the last month have made me feel more certain than ever of the wisdom of initiating a positive program of assistance along the lines indicated above. Reports from China convince me that the need for quick action is urgent."

Well, that's at least where I stand, and I hope everybody in this group, emotionally, is with me. There is no doubt about how the President feels. I felt it so important that I wanted to put it down in writing and two or three times while I read it to him he, "Grand," "Fine," "Bully." I mean, he - he - he - so on that thing, I thought, these people are coming down tomorrow, we'd first

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talk about sterling, what it means to us; we'll talk to them about what we might do in South America, and when I am talking about South America and Central America, I am talking and thinking in terms of five hundred million dollars, and I am thinking of the United States Government doing it right out in the open and getting permission from Congress to do so. There's a hundred million credit now in Brazil, and it's right out in the open. And everybody writes about redistribution of gold. I don't know any better way to do it and if we don't do it, and do it very, very quickly, we're out, that is all. And I have no plan - ah - (pause) having these people in, sitting around tomorrow, we will talk it over and see what they think. There's some smart boys coming down, and we'll see what they've got. But somebody's got to take the initiative. Certainly, I got a most hearty reception from the President. That's all I could ask for, and had an hour and a half with him, uninterrupted.

The other thing which I can't talk much about because it is - that's why Aubrey Williams isn't coming in - that is this new armament thing. The question of the new armament program for the United States, and in connection with that is the question of how we can use both Public Works and W. P. A., and would you (Mr. Bell), on that - Hopkins felt that he had at least forty thousand men working now for the Army and Navy - would it be very difficult to get those?

Bell: That's about right.

H.M.Jr: And he didn't know how many Ickes had, and the thought was the possibility of redirecting those men on something we might wear. The question is how much Hopkins has got, and how much has Ickes got, and Hopkins don't have - I'd like to go to the President, but what has Ickes got left available if we wanted to - well, say, let's say buy some land. He seems to think we'd have to go to him.

Bell: He hasn't any money left.

H.M.Jr: Nothing?

Bell: No sir.

H.M.Jr: Could he do any cancelling?

Bell: I doubt if he could get very much through cancellations. It's pretty well obligated. I gave him the last money last week. There will be some, but relatively small.

H.M.Jr: Do those reallocations go through your office?

Bell: No sir, they do not.

H.M.Jr: Where do they go?

Bell: They go directly from Ickes to the President.

H.M.Jr: Could you call up Burlew and tell him, if you trust me to the extent that if there are any reallocations coming in would he do me the courtesy of talking to me while Mr. Ickes is away? This week, between now and Monday? If anything comes in.

Bell: Uh huh.

H.M.Jr: Huh? I am sure he will do that because Burlew - I know he tells everybody. And I am the only Cabinet member that treats him like a gentleman, at Cabinet.

Bell: Uh huh.

H.M.Jr: But anything that is cancelled they can buy land with, can't they?

Bell: Well, under certain conditions; they can't buy it for every purpose.

H.M.Jr: Well, I'll .....

Bell: Put in more about it.

H.M.Jr: I'll tell you what we could do; you said eleven o'clock, didn't you?

Bell: Yes.

H.M.Jr: You come in at eleven, and Mrs. Klotz .....  
(talks very low.)  
Come in at eleven; I'll talk to you, see? Huh?

Bell: (Nods "Yes.")

H.M.Jr: Now - well, that's that. How far - I got through you, didn't I?

Lochhead: (Nods "Yes.")

H.M.Jr: Harry?

White: You remember that report that Kennedy sent, on his estimate of how our trade would be affected by various levels? He sent a rather lengthy report, made in his office. We made an analysis and criticism on that. Would you want that presented at the meeting, or done personally?

H.M.Jr: Well, if I did it, I'd do it without referring to Kennedy. If it's important - if it's important, see? I mean, I wouldn't bring him up, as an individual. But if you had something to present, Harry, on sterling, to sort of start the discussion off, I think it would be very easy.

White: I'll outline the situation.

H.M.Jr: You can read the memorandum for them to shoot at, if you don't mind doing that.  
(Nods to Mr. Gibbons.)

Gibbons: I have nothing today of importance.

H.M.Jr: Incidentally, Herbert Feis is coming, so we will have the State Department in. Huh?

Gibbons: (Nods "Yes.")

H.M.Jr: (Nods to Mr. Upham.)

Upham: Mr. Delano will be here Monday to be sworn in, and he is very eager, and his doctors are very eager,

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that it be a very quiet ceremony, and he wondered if he could satisfy the press by telling them later they could get all the pictures they wanted, but Monday they just don't want him to .....

H.M.Jr: All right, ....

Upham: He pretty nearly had pneumonia, but while he is definitely over the hump, they wanted .....

H.M.Jr: If he's so sick that he can't be sworn in, he'd better not come to the office. I mean, if he's that sick.

Upham: He's all right, but the doctors want him to be careful the first few days after he's been so sick; that's all.

H.M.Jr: Well, is he so sick that he can't stand up and do it publicly? I think it's very bad that he can't do it publicly; I think it's very bad. I mean, it would be misunderstood, and start an awful lot of gossip. I have had enough trouble. I think it's very bad public relations. I'd wait; if he's so sick that he can't have his picture taken, he'd better wait. Seriously. I'll not swear him in privately; I won't do it. I mean, I am not going to have a lot of more gossip, and lots more stories about it. Either the man is well enough to be Comptroller of the Currency, or stay in bed. I am not going to do it privately. If he wants to sit down at his desk from nine to five, he's well enough to have his picture taken. I am just not going to go through with it, that's all. Am I right or wrong, Herbert?

Gaston: I think you are right; I think he should wait until he's able to have his picture taken, and then.

Upham: All right.

H.M.Jr: You tell him when he's strong enough to have his picture taken, I'll do it.

Upham: Well, that's - I'm sorry to have that come out that way.

H.M.Jr: I think it's silly.

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Klotz: (Low)

H.M.Jr: If he can't stand up to have his picture taken, then he can't stand up - going up against Mr. Giannini, either.

Upham: I won't argue with you about it.

H.M.Jr: All right. What other good news have you got?

Upham: (Laughs) Well, Jesse Jones called me early this morning and had a little chit-chat about Anglo-California.

H.M.Jr: Yeah.

Upham: I gather that Herbert is sort of taking the position that Mr. Jones has encouraged him .....

H.M.Jr: Herbert Gaston?

Upham: No, Herbert Fleishhacker - that he doesn't have to resign because Mr. Jones encouraged him to think that he didn't have to, whereas the Board in San Francisco is pretty eager for Herbert to get right out.

H.M.Jr: What are you going to do?

Upham: Nothing; I think within a few days the Board will probably ask Herbert to resign. I think it will work out all right. There isn't anything; I just wanted to bring you up to date; that is all.

H.M.Jr: O. K., anything else?

Upham: No, I think not.

H.M.Jr: (Nods to Mr. Hanes.)

Hanes: I have nothing. I'd like to see you sometime today about some details in the Bureau; that is all.

H.M.Jr: (Aside to Mrs. Klotz.)  
Let's see, John, how we get along today. Let's see how we get along.  
(Nods to Mr. White.)



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- White: Is there going to be a final meeting or another meeting on Chen's stuff?
- Hanes: Tomorrow - I thought we were going to have a meeting sometime tomorrow.
- H.M.Jr: Well, the only thing tomorrow - I've got a big day tomorrow. I can do you fellows - I can see you Chinese boys at a quarter of twelve, if you want to come in.
- Hanes: Well, we will have something by a quarter of twelve. I don't think it will be .....
- H.M.Jr: Supposing you Chinese come in at a quarter of twelve.
- Olyphant: Eleven forty-five.
- Taylor: I don't know whether this makes much difference.
- H.M.Jr: (Speaks aside to Mrs. Klotz.)
- Taylor: I've got to be at Sumner Welles' office at twelve o'clock to meet this Peruvian who is here. I don't know whether that needs to interfere with this or not.
- H.M.Jr: Well, stay here ten minutes. We ought to talk it over in ten minutes.
- Taylor: Yes, it's a ten-minute job.
- H.M.Jr: Won't take more than ten minutes. All right. I tell you what you do, John. I won't get around to it. Pick me up at eight thirty tomorrow morning and we'll clear your stuff. Suppose you pick me up at eight thirty tomorrow?
- White: Wayne, is some concrete suggestion going to be made today, with the Peru ....?
- Taylor: No, I am - they have arranged sort of a meeting here in which Sumner Welles is going to give him some outside hell about Peruvian business and so on, and just want me to come over there and say, "How do you do, Colonel?" or whatever his name is, and then arrange to go on from there.

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H.M.Jr: He doesn't like eight thirty; he's got to learn.

(Laughter)

Taylor: That's late. (Laughter)

H.M.Jr: I have (words drowned out with laughter) tomorrow; otherwise it would be too late for me.

McReynolds: John, you'll have to learn to sleep faster.

(Hearty laughter)

H.M.Jr: Very good. All right. Where were we? Were we on Hanes' sleeping?

Taylor: I was giving a lecture to Harry on the side about Peru, but that is all. On the Peruvian thing, why, they've arranged a ceremony in which the Peruvian Colonel, or whatever his name is, will be given some hell about Peru in general.

H.M.Jr: All right.

Taylor: And I am supposed to listen to that, and then say, "I am glad to meet you Colonel, and when, at your convenience, do you wish to discuss silver with the Treasury?" or something like that.

H.M.Jr: O. K. Incidentally, Hanes, when you see me tomorrow morning, after your breakfast, will you talk to me about Phil Young?

Hanes: After dinner, you mean? (Laughter)

H.M.Jr: (Laughing) That's good, too. Tomorrow morning.

Klotz: He said what?

H.M.Jr: After dinner. All right. You all right?

Taylor: All right. That's all there is. Have you got any instructions on the Peruvian?

H.M.Jr: Nothing - to say howdy. Mac, Admiral Peoples' memorandum to me on procurement of aviation - I gave that to the President and in that is the Executive Order that the President had this one

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thing, of which Peoples was at the head of, and he asked me if that was still Executive Order six thousand and something. I'd like a copy of that for my files, and I'd also like to know whether that Executive Order still holds. Peoples gave it to me Friday.

And Harry, that thing you and Wais sent up to me on aviation, can I have a copy of that, please?

White: Yes.

H.M.Jr: And you held them to the last second, too, didn't you?

White: Well, we have stenographers with unequalled ability, I find, in the country over.

H.M.Jr: Anyway, can I have a copy?

White: Yes.

H.M.Jr: I left that at the house.

George? And George, analyze that (news clipping) for me, will you?

Haas: These are a few memoranda .... (speaking low)

H.M.Jr: You might bring that thing up this afternoon at two fifteen. There is something that goes out - maybe Mr. Bell passed on it.

Haas: We've got this; I've got it.

H.M.Jr: Have you got it? I mean, N. E. C. gives out an analysis of expenditures of seventeen million dollars - did you see it before it went out?

Bell: No.

H.M.Jr: Did you see it? The N. E. C. says I can't go on the radio until I get their permission. I say to them, they can't give out financial figures until the Director of the Budget or the Secretary of the Treasury sees it. They give out a statement, analyzing expenditures for the last five years, and I think the Director of the Budget or the

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Secretary of the Treasury ought to have the courtesy of looking at it.

- Taylor: R. F. C. - I forgot to tell you about the financing. All other things being equal, straight three years, seven-eighths, full exchange, no interest, to run. In other words, kill the interest with November first.
- H.M.Jr: And date it November first?
- Taylor: And date it November first.
- H.M.Jr: Will you talk to me again about it, tomorrow? I spoke to Randy Burgess about it yesterday, and he said exactly the same thing; that three years is within the limits of the President's .....
- Oliphant: Three years - yeah.
- H.M.Jr: Will you do it today, and again tomorrow? Burgess said exactly the same thing.
- Taylor: That's what Sproul thinks, and Jesse.
- H.M.Jr: I am counting on you for the machinery set-up.
- Bell: I understand there's been a question raised in the legal section - the authority of the R. F. C. to exchange.
- Oliphant: In regard to refunds - opposed to refinancing. I think it merely goes to a question of form, Dan.
- Bell: We are offering three hundred million dollars of notes.
- H.M.Jr: New notes?
- Bell: New notes, and we are accepting in payment only maturing notes, so it is an offer and purchase and sale. We only accept in payment the maturing notes in December.
- H.M.Jr: I didn't know that. I thought you were paying off in cash, and issuing new ones. That's the question I raised the other day. If you want to get the new ones you've got to own the old ones?

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Bell: That's right.

H.M.Jr: Well, I didn't realize that. I left it to you fellows, and I'll go along; I thought we paid off the three hundred million dollars cash in this new offer.

Taylor: It amounts to the same thing.

Oliphant: It would remove entirely this question that's been raised.

H.M.Jr: I have never done it this way before.

Bell: They've - they have done it privately.

H.M.Jr: And every time they've done it, it's been a failure.

Oliphant: It opens you up to criticism. They are very narrowly held now, aren't they, Dan?

H.M.Jr: I don't like it.

Oliphant: Very narrowly held, and it does open you to criticism.

H.M.Jr: If you fellows say it's too late, and I left it to you, I say, "No, I don't like it," but I'll .....

Bell: It's handled almost exactly like we handled our own refunding operations.

H.M.Jr: Oh no.

Bell: Well, but ....

H.M.Jr: No; now, Dan, you hold a note; we pay these fellows off in maturing notes, in cash.

Taylor: We'll pay off the ones that don't present, in cash.

Bell: Oh yes, sure.

H.M.Jr: We'll take this last note issue, and then, that brings up this whole question of rights, which I thought you didn't want. You pay these fellows off in cash, and no rights with it, an entirely new crowd comes in and subscribes. How did we do our last ones?

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Bell: Well, we offered notes for sale, and then gave the people who held the maturing notes the right to come in and subscribe, and pay for those subscriptions by tendering those maturing notes. If they didn't want to tender them they had the right to obtain cash for them.

H.M.Jr: Are we doing that this time?

Oliphant: Can a new outsider come in and buy?

Bell: No.

Oliphant: I think it's a little different. You don't know how much they have been spread around.

Bell: I think they are still going to be narrowly held at seventy per cent.

H.M.Jr: Well, it would be subject to the same criticism on our own.

Oliphant: Well, they are very widely held.

H.M.Jr: What I'd like to do, gentlemen, is follow exactly the same pattern as our own Treasury handles our notes.

Taylor: I think that's what we are doing.

H.M.Jr: Exactly the same?

Bell: Yes sir, exactly the same. Anybody that doesn't want to present their notes can get their cash.

Taylor: Get their cash and let it run to December fifteen.

H.M.Jr: But if they think they are going above par ....

Bell: It would be eight thirty-seconds.

Oliphant: Have you seen a distribution of the notes at present?

H.M.Jr: I know about what it is.

Taylor: If we were asking for any cash in addition, why, then you would - which you ordinarily would do - why, then you would have the maturing notes, and

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so on - give them preferential rights, which the Treasury has been doing right along.

Bell: Yes sir.

Taylor: And for cash, on a subscription basis, but there is no cash involved in this.

H.M.Jr: Since I've done it for Jesse, I want to do it exactly just the same as our own note issue - refund issue.

Bell: That's the way we understood it.

H.M.Jr: If Thurman Arnold wants to examine it, it's all right with me.

Oliphant: What?

H.M.Jr: If Thurman Arnold wants to examine it as a monopoly it's all right with me.

Bell: Some of these, I believe, are the old gold notes.

H.M.Jr: I'd like Herbert Gaston to receive the press and say this is being done exactly the same way as we do it in our own Treasury.

Bell: The rights have gone up a little; it was about four thirty seconds premium when we started discussing it, and they are now about eight.

(Mrs. Klotz leaves.)

H.M.Jr: All right. You check again?

Taylor: What?

H.M.Jr: You check again tomorrow?

Taylor: Every day.

H.M.Jr: George?

Haas: I have nothing.

H.M.Jr: Herbert?

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Gaston: I understand one of the independent agencies has lured away one of our best men. I don't know whether you want to mention it this morning. Morris Collins has gone to the Budget, from Accounts and Deposits.

H.M.Jr: Did he?

Bell: Yes.

H.M.Jr: What position?

Bell: As Assistant to the Director. He asked to be considered, and I went to all the other departments, and asked them to release their best men, and when one of my own men asked to be considered, I couldn't very well turn him down, having gone to all the others.

McReynolds: It's a question of ..... (speaking low.) Lee Martin went too.

Gaston: Lee Martin, from Procurement, from Reynolds' office.

McReynolds: He's one of the very best men, but he wanted to go.

Gibbons: I believe Dan is to be congratulated in getting Collins.

Bell: I think so too. I really hated to see him leave the Treasury.

H.M.Jr: What a pal you are.

Bell: We're getting some good men in the Budget. We won't have so much trouble filling Collins' place; we'll put Heffelfinger in there, but we'll have a little trouble filling Heffelfinger's place.

H.M.Jr: But Martin was a good man.

Bell: Yes, a good man.

McReynolds: Witman, who we'll put in his place, is also a good man.

H.M.Jr: What a pal. I'll bet you increased their salaries, too.



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Bell: No, I haven't increased a salary, on coming in to the Budget yet. They are all coming in at the same salary.

Taylor: Wait until they get a little experience.

Bell: Sure, after they are there and learn their jobs ....

H.M.Jr: Any other good news, Herbert?

Gaston: No, I think not.

H.M.Jr: Herman?

Oliphant: Nothing.

H.M.Jr: O. K.

McReynolds: Well, all this stuff about Jesse Jones is enlightening to me, because we have had to send a car over to get him and bring him down the last four or five days.

H.M.Jr: Has he started that again?

McReynolds: I just wondered - he's probably thought he's being gypped by the Treasury and he's trying to get it back that way. All they do is go up to his hotel and bring him down.

Treasury Department  
Division of Monetary Research

269

Date.....10/20.....1938

To: Mrs. Klotz

This is the cablegram which the Secretary mentioned in this morning's staff conference as not having been seen by the President. The Secretary asked that I give him the cable.

The cable is appended and copies made.

*White House*

MR. WHITE  
Branch 2058 - Room 200

DIARY OF HONORABLE SECRETARY  
OF STATE

RAW

PLAIN

London

Dated October 8, 1938.

Rec'd 8:45 a.m.

Secretary of State,  
Washington.

1144, October 8, noon.

FOR TREASURY FROM BUTTERWORTH.

1. In connection with the subject matter of my 1128 of October 5, 5 p.m., it is worthy of note J.M. Keynes should conclude a letter to THE TIMES with the following suggestion:

"In the circumstances of the moment I suggest that the balance of trade position and the net disinvestment in this country's foreign assets which is probably going on (about which we have as usual no adequate statistics) also needs particular attention -- not indeed by an aggravation of tariffs but by a new and now necessary machinery for linking up exports with imports so as to make sure that those from whom we buy spend a reasonable proportion of the proceeds in corresponding purchases from us. We can no longer afford to leave the barter aspect of foreign trade to look after itself".

It

-2- 1144, October 8, noon, from London.

It is safe to predict that in ensuing months this type of suggestion is going to come very much to the fore.

2. Reuter reports that a Czechoslovak financial delegation headed by Pospischil, formerly Governor of the National Bank, is expected to reach London today "to open negotiations concerning the economic reconstruction of the new Czechoslovakia".

3. With Paris closed and therefore no demand for dollars against offerings of francs the dollar has not been actively bid and the volume of trading has been small. The rate has remained around 4.78 5/16. Gold fixing of 257 bars at 145s.4 1/2d. constituted a premium of 1/2d and the British authorities gave a substantial part of the fixing. The British authorities indicated to the market that they were prepared to take francs at 179 but little business has transpired.

KENNEDY

HPD

RECEIVED  
 OCT 10 1938  
 FEDERAL RESERVE BANK  
 OF NEW YORK

RECEIVED  
 FEDERAL RESERVE BANK  
 OF NEW YORK  
 OCT 10 1938  
 Division of  
 Monetary Affairs

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE October 20, 1938.

272

TO Secretary Morgenthau  
FROM Mr. Taylor

Regardless of the technicalities which appear to surround modern conflicts, it is obvious that Japan and China are engaged in a bitter war. If an agency of this Government extends credit to the Chinese Government to enable that Government to purchase food, clothing or war supplies and fails to extend similar credits to the Japanese Government it is equally obvious that this Government has chosen to aid one of the combatants, and that the world at large and the combatants in particular will so interpret such an action. If, on the other hand, in a spirit of impartiality an agency of this Government should extend credit to both combatants on equal terms, this Government would then be in the position of underwriting a war, and thereby helping to prolong it to the extent to which this Government might make such credits available.

The nuance involved in an agency of this Government making a loan to a Chinese Government owned American Corporation, which in turn advances substantial amounts of money obtained from the American taxpayers on the security of a contract for possible future deliveries of tung oil does not in any way alter the fundamentals. The transaction is one involving responsible officers of this Government in a series of acts leading to the use of public funds for the purpose of giving financial aid to a belligerent.

While no one has ever been wise enough to predict the duration of any struggle of this character, the length of the present conflict

- 2 -

is particularly difficult to estimate, nor is it possible to evaluate the credit performance of nations engaged in armed combat. Nevertheless, it should be evident that the longer the combat, the more the credit, the greater the destruction of human and economic values and the greater the ultimate credit collapse. Certainly our own experience as a creditor would indicate that outright gifts to belligerents, even when these belligerents are on our own side, is preferable to disguising as credits our contributions to a cause which we have selected.

Many things have happened in the world since Congress last expressed itself on the subject of neutrality, it may well be the case that the people of this country would like to aid the Chinese people in their conflict and that if the questions were presented to them through their chosen representatives that they would vote to extend credits to the Chinese Government or to make a gift of some of our abundant wheat and cotton. However, in the absence of a specific expression of opinion by the American people on the specific points at issue, it is my conviction that any executive officer of this Government would stretch to the breaking point any authority hitherto delegated to him by Congress if he approved the proposed tung oil transaction, the wheat and cotton credits, or any other credits involving the direct or indirect use of Government funds to aid active combatants engaged in declared or undeclared war.

I strongly recommend to you that these and similar credit negotiations be dropped for the reasons which I have stated above.

Wesley Taylor

October 20, 1938

TELEGRAM (OVER WHITE HOUSE WIRE)

COL. MARVIN H. McINTYRE  
NELSON HOUSE  
POUGHKEEPSIE NEW YORK

PLEASE REMIND THE PRESIDENT THAT HE PROMISED TO SEE  
HANES BELL AND MYSELF ON MONDAY AFTER LUNCH IN CONNECTION  
WITH THE BUDGET AND TAXES STOP WOULD APPRECIATE HAVING  
THIS APPOINTMENT

HENRY MORGENTHAU JR

OC 25 1938



TREASURY DEPARTMENT

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PROCUREMENT DIVISION

OFFICE OF THE DIRECTOR

WASHINGTON

October 20, 1938,

MEMORANDUM TO THE SECRETARY

Re: Special Purchases of Clothing for WPA

The following is the summary of the clothing program, on which Procurement has been engaged in carrying out each phase of this program:

Authority

Letter from President to Administrator, WPA dated June 21, 1938 - allocating	\$10,000,000
Letter from President to Administrator, WPA dated July 16, 1938 - allocating	5,000,000
Letter from President to Administrator, WPA dated October 8, 1938 - allocating	750,000
	<u>\$15,750,000</u>

Purchases

Men's and Boys' woolen suits and overcoats, 1,100,569 garments or suits	\$ 8,726,003.09
Women's and Misses' woolen suits and coats 400,218 garments	1,528,368.24
Miscellaneous Women's and Children's clothing consisting of blouses, knitted outerwear, utility dresses, skirts and jackets, infants' and children's clothing, rainwear, and men's and boys' melton jackets	
Estimated.....	4,989,640.10
Freight, estimated.....	65,000
Total to date....	<u>\$15,309,011.43</u>

In the case of men's and boys' clothing, offers were solicited by letter from 1,800 firms on clothing on hand as of May 1, 1938. The Committee of Buyer Consultants was selected from Ed. Smster & Co., R. H. White Co., E. C. Lytton & Sons, Sears, Roebuck & Co., Wm. Filene's Sons Co., and the J. C. Penney Co. Offers were received from 666 firms accompanied by 3,000 samples. After selections were made, many firms being required to reduce their prices, 640 acceptances were issued.

In the case of the misses' and women's suits and coats, inquiries were addressed to 2,000 firms, also for clothing on hand as of May 1, 1938. A Committee of Buyer Consultants was selected from Henry Rose Stores (Sears, Roebuck & Co.), Wm. Filene's Sons Co., and the J. C. Penney Co. Offers were received from 378 firms accompanied by 4,139 samples and, after selections were made, 290 acceptances were issued.

A similar procedure was followed in the three phases as to the women's and children's clothing.

*H. C. Peoples*  
Director of Procurement



Thursday  
October 20, 1938  
10:42 a.m.

HMJr: Hello.

Operator: Jones. Go ahead.

HMJr: Hello, Jesse.

Jesse  
Jones: Good morning.

HMJr: What's this I hear about your going to Paris?

J: (Laughs) Talking to Paris.

HMJr: Oh. I heard you were going to Paris.

J: (Laughs) No.

HMJr: I don't know why you didn't invite me.

J: No. No. No, I - I'm still on the little matter that I mentioned to you about Portugal.

HMJr: Yes.

J: I was just checking to see whether there was any change in the situation since we had talked.

HMJr: No, I had them look it over and I would say - my best guess is that Portugal as of today is good for five million.

J: Yes. Well now, I just talked to this fellow - he - he was in a hurry to talk and he's coming over so it'll be another ten days or two weeks before anything happens.

HMJr: O. K.

J: He's coming over here to - to see what he can work out.

HMJr: All right, Jesse.

J: What's the news with you?

HMJr: Well, the news is this: - we - ah - it looks now unless there is some change - that we can sell a three-year R.F.C. note at seven eighths and ah - no extra interest I mean.

- 2 -

J: Yeah.

HMJr: And then -

J: No extra interest?

HMJr: No extra interest.

J: Yeah.

HMJr: And that, I should think -

J: It's at that way to go, huh?

HMJr: Well that's unless there's some decided change - the - the boys tell me seven eighths.

J: Any other news?

HMJr: Ah - nothing very much except that this whole question of what direction we're going on re- armament and all that.

J: Yeah.

HMJr: And it's pretty important but there's - there's got to be a lot of work to be done on it and ah - and ah - I think it's unfortunate that ah - that ah - Baruch rushes the papers with it.

J: Yes. That didn't do any good.

HMJr: And it makes it very much more difficult for the President.

J: Why certainly.

HMJr: Because he's not ready and - and he's - and it just forces his hand before he's ready.

J: That's right.

HMJr: And it's terribly important that ah - but ah - that we know what we are going to do before we shoot.

J: That's right.

HMJr: That's the most important thing that I know of and ah - ah - otherwise -

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J: Well, put me down for a date.

HMJr: I'll - I'll do that. Ah - are you going to be in town next week?

J: Yes.

HMJr: I've got a lot of visiting economists here tomorrow.

J: All right.

HMJr: So I'm tied up, but I would like to see you. I tell you, let's make it tentatively Tuesday. -

J: All right.

HMJr: For lunch, huh?

J: Fine.

HMJr: How's that?

J: All right.

HMJr: And if the issue goes well why I'll give you an extra portion of cheese.

J: All right. Well, (Coughs) I'll - I won't eat any breakfast then.

HMJr: (Laughs)

J: Goodbye.

## RE BUDGET AND ARMAMENT PLANS

October 20, 1938.  
11:00 a.m.

Present: Mr. Hanes  
Mr. Bell  
Mrs Klotz

H.M.Jr: What I wanted to tell you gentlemen - and I'll make a record as I go along - is this. This is very confidential. Give me a chance to gradually get in what I did in a day and a half. We're traveling so fast. This is what the President is thinking about. He's thinking about - well, might as well give you the whole story, but I don't want you to - this is just for you. He worked it out while I was sitting there with him Tuesday night. He's thinking in terms of our producing 15,000 airplanes a year for this country; give private industry 3,000 and we'll produce 12,000. He's thinking in terms of three shifts. He's thinking in terms of eight plants located around the United States, places where there are a number of other employees, like New York, Boston, Philadelphia, with the plant to be a few miles out of the city - one plant on the West Coast.

His original proposition to me was 500 million for Hopkins for the real needy, three billion dollars for airplanes, and a two billion dollar national defense tax. That was the original proposition Friday morning.

Bell: Two billion ...

H.M.Jr: ..tax.

He's very, very angry at Baruch. Said he never discussed - he discussed both things, but he never discussed them together, and in any case Baruch had no business to talk about it. Talked about airplanes and talked about taxes.

Bell: Army and Navy have been talking about it publicly.

H.M.Jr: Well, the President - well, the Army and Navy don't know what they're talking about, because they don't know this.

Bell: They've been talking about it for the last month.

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H.M.Jr: I know, but they don't know how far the President wants to go.

Now, Hopkins is up there, and the reason he isn't coming down is this. Hopkins says that if the President will give him the word he could start at once leveling the ground and building these plants. He can't equip them, but he can build them, provided that W.P. ... - Works - Ickes will buy the land. And of course, in many places they have Army reservations; don't have to.

The President is talking about a thousand anti-aircraft guns.

Hopkins is all excited about this thing, wants to get it. Says he can put a hundred thousand men to work. Now, what he says on this at once, and it's very true, is that the President's program - with all this work, that he can't employ more than a couple hundred thousand people on this. And what's going to happen to the rest? I think Hopkins is right.

Hanes: You mean on the plants themselves?

H.M.Jr: Well, on the construction. Until they've got them constructed. First they've got to make plans, then construct them. He said even if they construct it, if they employ a hundred thousand, that will be a lot - directly. The Germans only claim they have a hundred thousand people working in the plants.

Of course, I think the President is all mixed up on his prices. Talking about planes that will cost - he says the German planes cost \$15,000, we can build them for twenty-five. I think he's all wrong.

Hanes: German plane cost \$15,000 - those twin motor bombers? Whew! Great Scots alive! We built against the Germans in Argentine, and they were 40 percent under our price, and we got a net of \$120,000 a plane, just - when they were 40 percent under.

H.M.Jr: The - I said - the best figure I used was what - the English got 200 Lockheeds for 18 million dollars, plus the spare parts three and a half million - twenty-one and a half million dollars, which works out about a

-3-

hundred thousand dollars apiece. Then if you're going to build them in lots of a thousand, you'll cut that down some; cost very nearly - somewhere close to a hundred thousand dollars apiece.

- Hanes: They can build a modern bomber now in quantity at about \$30,000; but not quantity like we're building now - cost about a hundred thousand.
- H.M.Jr: I would say seventy-five thousand - I mean we're not far apart. The President's talking in terms of twenty-five.
- Bell: We're not building bombers now for a hundred thousand dollars. They're very small. The big bombers cost about \$285,000.
- Hanes: You're talking about the four-motor. I'm talking about the fighting bomber. The Germans are building about 300 a month in quantity.
- H.M.Jr: I want to give you people in strictest of confidence the inside where this thing is, see? Friday morning I'd have sworn I couldn't tell a living soul, and Sunday I read it in the papers. General Craig, very confidentially, is having lunch with me today, and I talked to him and he's terribly excited because he knows that what is being told the President is impossible. He said, "What you going to do, build a lot more wooden ships, store them up there in Newark Bay?" He said, "You going to have a lot more wooden ships, the way we had in the Navy during the War and never used them."
- He's coming to lunch and, very confidentially, next week I'm going to school with General Arnold.
- Hanes: Do what?
- H.M.Jr: I'm going to school with General Arnold, new head of Aviation. I'm going to spend practically every morning, beginning Monday morning.
- Hanes: I wish you'd take that flight of 20 minutes over here, see what can be done.
- H.M.Jr: Maybe we will. I want to go to Langley. General Craig doesn't want me to go to Langley. Wants to keep me

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here first. He said, "If you go to Langley you get one picture; you go out to Dayton, you get another picture." He said, "If you want me to do this for you, I want to give it to you here first."

I'm going to put myself in the hands of General Craig. I mean - then - I mean I asked him to map a schedule so I can go to school and learn what this is about. I said, "I've got to raise the money, and I want to know what it's all about." See what I mean?

Hanes: Sure.

H.M.Jr: So I'm spending a couple of hours a day on it, beginning Monday, until I've learned this thing; at least learned what the Army wants.

The President said, "As far as Navy is concerned, two hundred or three hundred planes is all they can use."

But Craig said last night - he said, "What are we going to do with fifteen thousand planes?"

Bell: You haven't got the Army, the aviators.

H.M.Jr: Said, "Who you going to fight, what you going to do with them, with three thousand miles of ocean?"

In other words, what I'm trying to get at - I want to get, at least as far as I can - at least get what the Chief of Staff thinks. The President just takes a piece of paper like this, works it out on there, and says, "That's what we're going to do." Hopkins says, "Well, I can do that."

I want to let you know - I can't over-emphasize the importance of this being confidential to anybody in this room - the thing all is in the air. When I talked to the President about taxes, he didn't seem interested. Now this is what Hopkins said. And get this. In the first place, he grits his teeth - just remember what I said two years ago - he said, "I don't care what anybody says, I want to reduce the rolls before election. I'm not going to let them say that I'm just playing politics."

Bell: Hopkins said that.

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H.M.Jr: Yes. And Mrs. Morgenthau said last night, "It never enters his mind, what about these poor devils on the rolls, do they need the work or don't they?" Well, he's going to reduce, with a nice gesture.

You (Mrs Klotz) remember what Mrs. Morgenthau said before me.

Klotz: (Nods yes)

Bell: Well, he's never thought, I don't think, the last two years in terms of the people.

H.M.Jr: Neither do I.

Bell: Always in terms of projects.

H.M.Jr: Dan and I for two Decembers running are the people responsible for increasing the rolls. For two years Danny and I are responsible for increasing the rolls before Christmas. And you most likely - you've got to take my word for it - the fellow that's always taken the initiative the last two years to lay the people off is Hopkins. You've got to take Dan's and my word that that's so. Is that right, Dan?

Bell: That's right.

H.M.Jr: And our written record shows it. And he's going to do this now and he's most likely going to stay within the figures up to the first of March, unless he can use this as an excuse, see?

Bell: Uh-huh.

H.M.Jr: Therefore, let's find out. And I'm going to be as intelligent as I know how. And as I say, I'm going to school with General Craig and General Arnold, and I'm going to get this thing: what does the Army want? Now we've got a good General Staff.

The President himself says that outside of what the Navy wants, plus some new carriers - he's only talking about two new battleships next year, possibly some more airplane carriers, and possibly some more Transatlantic transports which can be converted into air carriers. But as far as the Navy is concerned, he said they've got enough - I mean within reason.



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Bell: They've got about all they can handle.

H.M.Jr: They've got all ....

Bell: Close to 800 million dollars this year.

H.M.Jr: Got all that our yards can handle.

Bell: Sure.

H.M.Jr: Now, this thing - as I say, one of these times - fortunately, I've got my health back again; I was pretty down and out after this Munich business and what went before. But I got my balance back again and I've been traveling awful fast with the President. But I want to be intelligent about this thing, see? And I want you fellows to know what's happening.

Now, when I tried to get the President on the taxes - he hasn't got anything in his mind, see? See, John? He just doesn't know.

And this is the thing. That is, this is the program the way Hopkins looks at it. He said - my figures aren't quite straight, neither are the President's - the President said - just make - just follow me - he said that Ickes had a billion. Didn't Ickes have a billion and a half?

Bell: Well, he had a billion and a half, but he had to get the last 500 million through the sale of obligations.

H.M.Jr: All right. Well, let's just say Ickes - how much has Ickes contracted for now?

Bell: Well, it's - I'll have some figures at that meeting today, but I think it's less than 175 million.

H.M.Jr: Well, that isn't - well then, how much is he committed to?

Bell: 550 million.

H.M.Jr: 550. Then the President asked what the cities put up, the municipalities, on the matching.

-7-

Bell: Well, the 550 includes both loan and grants, and the loan is very small. So say 500 million is the 45 percent; the cities would put up about five also.

H.M.Jr: Give me this - when they get through, Hopkins gets a total this year of Federal spending of four billion eight. He takes the Ickes money. Then they added - the President did the same thing - plus the loan and grant. Said he's down for two billion three. And they total it up and get a figure of four billion eight.

So this is what Hopkins says to me: "I'll take two billion dollars for next year, plus 500 million for Ickes, or two and a half billion, which is a saving of a billion eight" - with the idea that the 500 million that Ickes gets would all go to the Army and Navy, see?

So this is what I told him, where you and I stood, the three of us. I said that we told the President a billion and a half in his January 3 message for relief. Isn't that what we said?

Bell: That's what he said.

H.M.Jr: Who?

Bell: We put no - the President stuck that in.

Hanes: You're right.

H.M.Jr: I seldom travel so fast. I said a billion and a half for him and nothing for Ickes - that's what I said - plus 500 million for Agriculture gave us a total expenditure of seven and a half billion, and I said I recommended to the President he go before the country with a total expenditure of seven and a half billion, a five billion dollar tax program, or two and a half billion dollars deficit; that I could stand that; then that he should say to Congress, "If you want anything more above that for national defense, anything else, give me a tax."

So I says, "Harry, will you take that?" and I says, "Will you agree with me on that?" Harry says, "I'll be delighted to take that." That was yesterday

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morning, see?

Bell: Uh-huh.

H.M.Jr: So I said a billion and a half for Hopkins, 500 million for Agriculture, nothing for Ickes, because that's what the President told me Friday morning: nothing for Ickes, seven and a half billion, and anything above that, if it's going to go for airplanes, whatever else - but if it's in there so it sticks out, then we can have a national defense tax. Does that check, John?

Hanes: That's exactly what you said to him.

H.M.Jr: I told that to Hopkins and said, "Hopkins, how far apart are we?" He said, "We're not apart at all."

But again - you know, we keep - see, an hour and a half with the President, then at 20 minutes to 11 he says, "Come in now, we'll talk about it all over again." So he starts all over again at 20 minutes of 11 Monday night. Didn't get home till 12. Then all the way up, all yesterday morning, Hopkins bing-bing-binged at me, see, trying to find out where I stood. Then I said, "That's where I stand."

Now, that's why - and then the President - you (Klotz) send McIntyre a telegram: "This will serve as a reminder that the President said he would see Hanes, Bell, and myself Monday after lunch. Would appreciate your bringing this - I'd appreciate your reminding the President."

Klotz: It's repeating.

H.M.Jr: What is it?

Klotz: "This will serve as a reminder that the President said he would see Hanes, Bell, and myself ....."

H.M.Jr: Well, then - "Please remind the President that he promised to see Hanes, Bell, and myself at two o'clock on Monday on the budget and taxes."

Bell: This is a continuation of that conference of last ....

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H.M.Jr: Yes. Now, what I want to do is..... Now, you see the way Hopkins' mind is working; he's building up a total Federal expenditure, plus the loans and grants, you see, and he's arrived at a figure of four billion eight, and then he says, "Now it's wonderful, we cut that down to three billion dollars. That means we'll save a billion eight this year, see? We cut it down to three billion dollars and we're saving a billion eight this year." And he adds in that figure what the municipalities put up, so when we go to see the President I want that on a sheet of paper, and say not on an outgo of cash, but what the Government will spend is so much on a budgetary basis. Now, to match Ickes, add down at the bottom "Contributions..." - so much, see?

Bell: States.

H.M.Jr: Yes. Now Harry claims he's getting two or three hundred million dollars worth of contributions.

Bell: Yes.

H.M.Jr: What?

Bell: I guess so.

H.M.Jr: We'll say, "This is what - this is what we're doing," and then at the bottom, "Contributions to public works program, so much; contributions to WPA, so much." But only cash. I don't want rental on trash baskets. Once went into contributions and found that the contributions - what was it?

Bell: Waste baskets.

H.M.Jr: They paid 25¢ a month rental for waste baskets. That was the contribution.

Bell: I think that their figures still contain items like that, and you can't get strictly cash. Services are in there too.

H.M.Jr: But certainly the Ickes cash is on a straight basis.

Bell: That's right.

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H.M.Jr: What?  
Bell: What's right.  
H.M.Jr: The Ickes thing.

And we might have a trial on that this afternoon, because maybe Hopkins and the President are getting that from this crowd; feeding this to him. And I'd like to just put up - I'm not going to say anything about this plane business or the rest of it. I'm going to say just what we said to the President, and what's happened since then is none of their business as of today, because it's too confidential and too much up in the air. I'll say, "Gentlemen, this is the picture we gave the President Monday a week ago."

But in that thing I'd like to have on a budgetary basis what we spend for public works and relief - what we - pump-priming. That's what the President keeps calling it - pump-priming. They're all wet on their figures, and I haven't yet got it at my fingertips to answer them. They're using a figure of four billion eight. They say, "We save a billion eight, spend three billion. See how good we are."

Now, do you get - now, I'm all right on what I told Hopkins on the seven and a half, am I not? I haven't changed.

Bell: No, that's right.  
H.M.Jr: All right.  
Hanes: That's exactly what you said.  
H.M.Jr: Then I'll have - by Monday afternoon I'll have a story from Craig as to what he thinks he needs to defend this country against an aggressor. That's all I want: what does Craig, the General Staff, think they need to defend this country against an aggressor or any group of aggressors?

Now also very, very much in this room, Ambassador Bullitt comes back and he says the thing to do is to help France and England if she wishes to build plants

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in Montreal across from Niagara Falls, across from Detroit, to produce a thousand planes a month. And Mr. Monnet, whom Bullitt suggested and Daladier OK'd, landed Tuesday in this country on that mission, and that's what these stories are about French loan and everything else.

Well, when I got to thinking it over, talked it over with my wife and son, they pointed out to me the danger - Bob saw it first - of having on the Canadian border three plants which could produce a thousand planes a month. Now, it sounds very silly today, but how long do we know that Canada and England are going to be our allies?

And the President, when I first said that - he said - he laughed, but then he said, "All right, I'll tell you a story right along that line." He says, "Napoleon had a general who - a peasant, fellow by the name of - of ....." - what's the name of the ruling family of Sweden?

Hanes: Bernadotte.

H.M.Jr: "... Bernadotte. He made him a general. Always suspicious of him, but such a good general that he made him a marshal. And then when he came around to getting rid of the people that he was suspicious of, he thought he'd make him King of Sweden. Then, after one of his great defeats.." - President couldn't remember which one - "...Napoleon sent word to the King of Sweden, former Marshal Bernadotte - he said, 'Now, I need a breathing spell; I want you to land on northern Prussia, help me, march against the Prussians, help me lick them, in order to give me a breathing spell.' And the King of Sweden, ex-Marshall Bernadotte, sent word, 'I'll land with my troops, I'll be glad to land.' And he did, but he joined the Prussians and licked Napoleon."

So - it's a nice story, it illustrates the point - so I filed a three-page memorandum with the President why I'm one hundred percent opposed to our doing anything. And as White points out, for every million dollars that you take out of France - it just makes their foreign exchange that much worse; that if they're going to do this thing, they'll have to do it the way

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the Germans do it, do it inside of France, help their own unemployment situation. Said they haven't got the money. If they - certainly Congress isn't going to permit me to help France when they owe us that debt. It would wreck them - I mean their internal economic picture. It would be a target for the German bombers to come over to make Canada a strategic point to be bombed.

To show you - this morning - I mean this confidential cable comes in: "It looks as though England has a deal with Japan: 'Take Canton as long as you leave the bondholders of the Canton-Hongkong Railway alone.'" That's what the cable said yesterday: "Looks as though they had a deal. 'What about the bondholders of the Canton-Hongkong Railway?' Said, 'They've got nothing to worry about. All been taken care of.'"

So you just don't know what happens. But I don't want twelve thousand planes being manufactured in Canada, where they take our mechanics, and where we're short enough of good mechanics. If we're going to do any production, we need every airplane mechanic we've got, don't we?

Hanes: Short all the way through the industry now. Can't get them.

H.M.Jr: And if we're going to quadruple or multiply by ten our production, go from two planes a day to fifty planes a day - that's what the President is talking about, fifty planes a day.

Bell: Is that our production now?

H.M.Jr: Well, it's very - produced 3,600 planes last year.

Bell: Ten a day.

H.M.Jr: Well, now - well, ten a day. Ten a day, yes, was our production for the whole country.

Hanes: Of course, that includes all the small planes, none of which is any good for our purposes.

H.M.Jr: Everything. I know. So he wants to multiply by five.

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But I think it's just cock-eyed. I told that to Bullitt yesterday. He said - he was furious. I said, "I'm sorry, Bill, I can't go along with you."

So now you've got about the whole story and, knowing that, I want you to put your own brains to work, because I consider it the number one thing. We don't want the President to make a mistake; it affects us violently, first on the budget and second on the tax program.

But you know everything I know now, and you know just exactly where the President stands on this whole thing and where Hopkins stands. And Hopkins is staying up there to be sure if anything happens he's in on it.

Bell: (Laughs)

H.M.Jr: And - well, that's the story, and we've just got to go to school - at least, I do, talking for myself - to find out what we do want. And somebody has given the President a lot of misinformation, talked to him; he's just all wet on it. But with that in mind, please do your heavy thinking.

You're (Hanes) coming this afternoon, aren't you?

Hanes: 2:30.

H.M.Jr: 2:15.

Bell: 2:15.

Hanes: Was it 2:15? Yes, I'll be here.

H.M.Jr: Yes. But I'm not going to tell these boys this afternoon anything about this.

Bell: Yes, O.K.

H.M.Jr: Because it's - well, it's just too confidential and it's too much up in the air. We don't know.

Hanes: Who are these people coming this afternoon?

H.M.Jr: This is the National Resources Board - Committee, plus Eccles. This is what the National Resources wants - a Fiscal Committee.



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Hanes: Fiscal Committee.

H.M.Jr: You be here 2:15 (to reporter).

Bell: Who's coming, do you know, from the Board? That group didn't intend to come.

H.M.Jr: Old man Delano and Ruml.

Bell: Oh, I see.

H.M.Jr: Let's give them the same shock we gave the President, without - just let them take it and see how they react.

Bell: Suppose this will be in the papers next week too.

H.M.Jr: Well, if it is, there won't be any more meetings. I'm going to open the thing by saying that this thing mustn't be - is in the strictest secrecy, and if there are any leaks I won't have any more meetings.

Hanes: Do you want to discuss the tax program in conjunction with this?

H.M.Jr: Yes.

Hanes: I mean the specific - going to be specific?

Bell: I'd keep it sort of general, say, "What we going to do? Raise taxes? If so, how much?"

Hanes: Keep it on the general side.

H.M.Jr: After Bell gets through I'll turn to you and say, "John, if we've got to raise one, two, three billion dollars, how we going to do it?"

Bell: Have several plans.

H.M.Jr: "How would you suggest that we raise it?"

Hanes: As Danny says, if you're going to open us up now very wide open, that's got a lot of dynamite in it...

H.M.Jr: Well, that's all right.

Hanes: ...if they spill the beans.

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H.M.Jr: Well, if they do, I can't help it, but ...

Bell: That'll be one way to get rid of them.

H.M.Jr: I'm going to say to them, "We'll try it. Never any leaks in the Treasury happened for five years. Now you people have asked for this. The first time there are any leaks, why, I'm sorry, gentlemen, I won't meet again."

Klotz: Mr. Morgenthau, I asked Eccles to come, and who arranged for the other two?

H.M.Jr: I did.

Klotz: I know I didn't.

H.M.Jr: Just check ...

Klotz: You have a meeting, and ....

H.M.Jr: Just check that Frederic Delano and Mr. Ruml are coming at 2:30.

Klotz: 2:15.

Bell: 2:15.

H.M.Jr: 2:15. So that, I would say, is the story, and at least you know where the President is as of last night - or night before last, I mean. I personally - I'm all bucked up over this thing, because I think that this thing can be done and done right; I think he can go to the country with it, I think we can raise the taxes, and I think instead of having a four billion dollar deficit there's a chance of cutting it down maybe to two. And besides that, I'm tickled to death the President is thinking of making this country so strong that nobody can attack us. I'm not interested in attacking anybody else, but I want to be so strong - oh yes, the other thing he said is that we want enough planes to take care of the whole South American continent too, to be able to supply them with as many planes as they need.

Hanes: Getting - talking now about long-range flight planes.

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When you get up over two thousand miles' range, then you're talking about something like a flying fortress, talking about something - take a tremendous plane to carry the gasoline. That's where your trouble comes.

- H.M.Jr: Well, I don't know who he's been talking to, but he hasn't been talking to General Craig, that's a cinch.
- Hanes: Anybody that knows anything about airplanes ....
- H.M.Jr: Well, I think he's talking too much to Bullitt.
- Bell: General Craig is the one he should talk to. Best Chief of Staff we've had in a long time.

## A. CHINESE AGREEMENT

October 20, 1938.  
11:45 a.m.

Present: Mr. Hanes  
Mr. Taylor  
Mr. Oliphant  
Mr. Foley  
Mr. White  
Mr. Lochhead

H.M.Jr: Well, who's teacher?

White: Well, we just left the conference at which there were Mr. Chen, his associates, and their lawyer. We were going over from their angle the contract which he has drawn up, and there were some rather important points there that they were discussing - make a substantial difference in what the price would be - and that's the point we were at there.

But Mr. Hanes has outlined the machinery, which I think he checked with Ed Foley, from the consumer's angle, and we're not far from getting together on the contract.

H.S.Jr: Well, Ed, give it to me while we're waiting. What's the procedure?

Foley: The corporation has been organized, as you know. It's a New York corporation, and certificate has been filed.

(Hanes comes in)

In so far as the corporation is concerned, they're waiting for the Chinese to tell them the directors and personnel and how the stock is to be held, whether it's to be some kind of a nominee and voting trust or whether to be held directly by the Republic of China. Mr. Hanes has the mechanical operation for financing the trading corporation set up, and the only thing that isn't worked out finally is the distribution of the oil on the part of the trading corporation after it's been brought into this country.

H.M.Jr: Well now, I'm a very simple-minded country boy. Will somebody take a ton of tung oil after it's collected and explain to me the process, what would happen to it, starting in China?

Hanes: Well, perhaps we better go back to the organization - we'll have to start with the organization of this

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American corporation which is owned by the Chinese Government. That corporation contracts with some appropriate agency in China - just how that's going to be done is up to the Chinese - for the collection of this oil and for the transportation of the oil to the seaboard. That oil is then transported to America for the account of the Chinese corporation owned by the Chinese but of American registry. That corporation then will proceed to make a contract with our distributors in this country, and that's the - there's the point where we have stalled for the moment, because we're trying to do it with the least possible upset to the existing machinery in the American market. Presently that oil is brought into this country by about forty-seven importers, the largest of which we have been in communication with. That's just simply a barter, import and export transaction.

H.M.Jr:

A barter?

Hanes:

Well, it's a - simply a negotiation between our American importers and the Chinese for the purchase from private individuals in China of this tung oil. And they have a machinery set up over there, our people - the extent of this we do not know, but our people have a machinery set up over there for the purchase and concentration of this tung oil at given points. At Hankow - there's 30,000 tons concentrated in Hankow now, belonging to both the Chinese corporation and the American importers who have purchased that oil and have means of storing it on the seaboard in China.

Now, as far as we have gone in the make-up of the machinery in this country - in order to keep it - visualize bringing the Chinese shore to California; in other words, up to the point we get the oil to this country, there is no change in the status of producer - production or transportation. So if we can, conceive of it as bringing the Chinese shore to California and then saying to our importers, "Instead of your negotiating for this oil in China, you are now able to negotiate in our own country." So we're going to - in other words, this corporation is going to do the importation, collection, so forth, and we're now ready for working out a machinery for distribution which will not upset the American market.

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Our plan, in rough, contemplates the following: The Universal Trading Corporation, which has already been incorporated, a United States corporation controlled by the Chinese Government, will make a contract to purchase from the appropriate Chinese agency minimum yearly amounts of wood oil over a five-year period beginning at 50,000 tons a year and increasing 10,000 tons annually until the fifth year 90,000 tons is imported, if they can produce it. The Chinese agency in addition would agree to offer all available wood oil in excess of this minimum amount or amounts to the corporation for first rejection. In other words, if the production is higher than that, they offer it to us for first rejection. The Chinese corporation would pay to the Chinese agency immediately a percentage - we've set down an arbitrary figure of six cents a pound.

H.M.Jr: Who would pay to who?

Hanes: The corporation; that is, our corporation - the Import-Export Bank, it would be, if we just cut across here for a moment; make it simple by saying the Import-Export Bank would advance to the Chinese Government, cutting out all intermediaries now, an amount - say, six cents per pound, for the life of the contract. That would mean that this total contract for sales of 700 million pounds over a five-year period - six cents a pound would be \$42,000,000 which the Import-Export Bank would advance, or approximately 50 percent of the purchase price.

H.M.Jr: To ...

Hanes: To the Chinese Government.

H.M.Jr: Well, let's just not even say Chinese Government. Do they advance that to the so-called Universal Corporation?

Hanes: That's right, they advance that to the American corporation. And one of the stipulations in the contract is that that amount, about \$42,000,000, is to be spent in this country for merchandise by the Chinese corporation - Chinese-owned corporation, the Universal Trading Company. Is that clear up to that point?

H.M.Jr: Yes, that the Export- - is it the Export-Import? I always forget.

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White: Export-Import Bank.

H.M.Jr: Export-Import is going to loan six cents a pound to Universal.

Hanes: That's right, for future delivery of tung oil. Now, that price - of course, these are details which have got to be worked out; now, I'm going to skip the details about how we arrive at a base price and how often that base price may be changed, because there are strange conditions which might come into effect there. As I outlined above, the total contract calls for 700 million pounds, and we're advancing six cents a pound, or \$42,000,000.

As security for that loan, the Import-Export Bank would have all the inventories and other assets of this Chinese-owned American corporation. Payments will be made out of the sale by the corporation of wood oil in pro rata amount from the proceeds. For instance, if one-half of the contract price had been advanced on the sale of the oil, then one-half of the proceeds would be paid back to the Import-Export Bank.

H.M.Jr: May I interrupt you there.

Now, Wayne, you as a director of the Import-Export Bank - are you with this plan so far - I mean as to this advancing of six cents?

Taylor: I think the only way you can do it is to use this corporation. I don't think you can bring in other American corporations.

H.M.Jr: Well, but I mean as this plan is outlined - before you leave, I want to know - I mean are you ready to recommend this to Export-Import bank, that this procedure be followed?

Taylor: I think it's - going as far as I have with it, I don't see how you can recommend any other procedure.

H.M.Jr: Well, that doesn't answer me. But I mean - I mean as to this method - I mean I just want to know, is this method of getting the Export-Import - without getting into details; I haven't gotten the details - to advance half the price of this thing on a five-year basis - I mean that method of doing it - I mean are you ready to recommend it?

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Taylor: I think that's the only method you can employ.

H.M.Jr: Then you are ready to recommend it?

Taylor: What I said is that I think that's the only method you can satisfactorily employ.

H.M.Jr: It might be the only method, but I might still say, "I'm not ready to recommend that method."

Taylor: Well, I don't - I don't understand the question that way.

H.M.Jr: The question I'm asking: is this the method which you're recommending?

Taylor: If the policy of the Government is to do this, I think this is the method to employ.

H.M.Jr: I'm getting back to Wayne Taylor as part of the Treasury and a director of the Export-Import Bank. Does Wayne Taylor recommend this? I'm asking, do you recommend it to me?

Taylor: As a method?

H.M.Jr: As something to do.

Taylor: I'm not ready to answer that.

H.M.Jr: No, as something to do. I mean I don't want to have it all sewed up and then have you say - well, if I ask you to go over and carry the ball for the Treasury in the State Department, I want to know whether you can carry enthusiastically this method.

Taylor: I'm not ready to answer that, Henry.

H.M.Jr: Well, what would be a reasonable time to ask when you would be?

Taylor: Oh, couple days.

H.M.Jr: Well, I mean - will they be ready before a couple days?

Hanes: Well, the Chinese, as I understand it - the Chinese are ready to move now.



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H.M.Jr: Couldn't you give me an answer tomorrow, Wayne?

Taylor: I think possibly.

H.M.Jr: Yes, because I'm pushing - I mean because this has been in the air now ever since before I left for Europe. What? I mean because I don't want - I want to know, in the family, is - I'm asking you people to recommend something to me so that I can say to the President, "This is what the Treasury recommends." Then, if it's up to you to carry it with the State Department or anybody else - I mean I just want to know, is this unanimous? If not, why not? See? Do I make myself clear? I'd like to have that tomorrow.

Taylor: All right.

H.M.Jr: What?

Taylor: That's all right.

H.M.Jr: I'd like to have it tomorrow, because then - if you don't think this is the way, give me an alternative, see? Wayne?

Oliphant: He said it was clear this was the way.

Taylor: What?

H.M.Jr: No, I'm - I just want - I wouldn't pick you out if you weren't leaving today to go over there, because I just want to know.

Lochhead: As I get it, Wayne, you're willing to recommend the method; it's a question whether you recommend the loan.

H.M.Jr: That's right. He puts it.

Taylor: Well - I mean after all, this is my method that I gave to you before I left for Chicago, so that there's no ...

H.M.Jr: Let's put it in Lochhead's terms. Do you recommend the loan?

Taylor: Well, that's what I would - I say I'm not prepared to tell you.

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H.M.Jr: Well, I think you ought to be able to answer by tomorrow.

Taylor: Right.

H.M.Jr: Thanks.

(Taylor goes out)

Hanes: I was assuming that we were all agreed that we were trying to work out a procedure - just let's cut across, call a spade a spade - we're trying to work out a machine to get some money into the Chinese Government. That's what everybody is agreed on. We want to get it to them as fast as we can. Here is a method which will get it there - get it there today or tomorrow, if they will agree to it.

H.M.Jr: I read my letter this morning, which is my Magna Carta on my foreign policy as far as I'm concerned, and the President didn't give me back the letter. No, I mean I'm just - as I say, I didn't want to put the screws on Wayne, but I've been waiting for three months to get the answer on this thing, and I want to know. I mean you (Lochhead) put it. This is the method which he recommended, but does he recommend that we make the loan? And I don't see why he needs more than 24 hours to say "Yes" or "No." Do you think that's unfair to ask him?

Foley: No, if he doesn't know tomorrow he'll never know.

White: Or yesterday.

Foley: Or yesterday.

Oliphant: He knows now.

Hanes: I don't know what the argument is about, because it seems so clear to me we're trying to get some money into China, and we all realize that this is not a sure thing, it's not a good loan, so far as that goes. For Heaven's sakes, we're not trying to make a good loan, we're trying to safeguard what we are lending, what we made our minds ....

H.M.Jr: I don't like to talk when Wayne isn't here, but what

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I'm trying to find out, been finding out for three months - Wayne is, as far as I know has been, opposed to this. But I don't want to go over and say to Mr. Hull that I recommend this, or to the President, and say, "Yes, but Wayne Taylor is opposed to it."

Lochhead: As I gather from speaking with ....

H.M.Jr: Weren't you (Hanes) aware of that?

Hanes: That he was opposed to it?

H.M.Jr: Yes.

Hanes: No. First I thought of it. He hadn't said anything about it yesterday when we talked about this for an hour.

Lochhead: In talking the last several times with Mr. ...

Hanes: In other words, I passed that ....

H.M.Jr: Well, I just wanted to know where he stood.

Lochhead: May I say, I think what I gathered there - that Mr. Taylor as a director of the Export-Import Bank - the point is, is this absolutely a safe loan, just the same as you make in an ordinary bank.

Hanes: No, it's not. Nobody ever thought it was.

Lochhead: As I say, if there is anything further, outside of that - he doesn't want to vote on that basis.

Oliphant: We've known for months ...

H.M.Jr: Well, I don't want to - well, after all - well, there's no use ....

Oliphant: Now, I want to mention an item here.

H.M.Jr: Well, let's just let Hanes finish.

Hanes: I want to go back. We were trying to devise an alternative plan. As I understood from you (H.M.Jr), Mr. Welles said that he would not have any objection if this loan were made to an American corporation.

- H.M.Jr: Well, I made that suggestion to him. He said, "It would be just none of our business, wouldn't concern us."
- Hanes: Say an American corporation which is owned by the Chinese - would it come under his category as a subject to object to?
- H.M.Jr: I don't think so.
- Hanes: Don't think so. Then if that's not objected to, then the alternative is not worth mentioning, because I think, and I take it from Herman that he thinks, that if we do anything here that's going to bring these importers into a conspiracy, we're aiding and abetting in something that we shouldn't be a party to, shouldn't let them be a party to.
- Oliphant: Got a statute we've got to watch.
- H.M.Jr: What I had in mind - I didn't know whether it was legal or not. Let's say - I don't know - let's say the Paint and Varnish Institute is an incorporated institute, and let's say for argument's sake that they can merchandise under their incorporation, that this loan of the Export-Import Bank would be made to this paint institute and that they in turn would parcel the thing out, see?
- Hanes: Herman thinks that would bring them into conspiracy to violate the Antitrust Act, and that's the reason why we shy off. I've got a plan set up which would do just what you're saying through the individual or collective - but that - Herman says that would bring them into a conspiracy.
- H.M.Jr: Well, we don't want to set up any examples so they can say, "Well, if the Government fathers this, what's a matter of a motion picture industry, what's the difference?"
- White: Be a poor case too.
- H.M.Jr: All right, we can't do it that way. Then it gets down to this thing. Christ Almighty! - we've been talking about this thing for three months, and up to now Taylor has been opposed to it. Now let's find out tomorrow whether he is or isn't, so these poor Chinese know where they stand at. I want to know. I want to know

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where they stand. Hell - I don't want to kid them one minute.

Hanes: Well, that brings us up to the last point, which, as I told you before, we haven't yet solved, and it makes necessary our talking with somebody in the trade to find out some few facts that we'd like to find out. And I'm ready to talk to those people whenever I get a clearance here that this is approximately the plan we want to follow. I don't want to go ahead and talk to them until we're ready to say that we're prepared to do this thing.

H.M.Jr: Well now, will you do something for me between now and midnight? Will you get hold of Jesse Jones and explain this thing to him and ask him whether he's for it or against it?

Hanes: Yes, I will.

H.M.Jr: Will you? Tell Jesse I'd like to know; that this is what we're proposing to do, we're proposing to make this thing, and is he for or against it? Is that crowding you a little bit?

Hanes: No, no, I'll get it this afternoon. Can't do it until late this afternoon.

H.M.Jr: Well, get hold of Jesse and tell him, and is he for or against this thing? Let's just see - well, you're handling this thing, aren't you? I mean I just was thinking about Taylor. Take Taylor with you, then there is no question of going behind Taylor's back. The two of you go over and see Jesse. That's the answer. The two of you go over and see Jesse and say, "This is what we're proposing to do." I'll call him up and say I'd like him to see the two of you. What time can you ...

Hanes: That's up to you, because we've got a meeting here at 2:15; after that meeting - right after that meeting I'll be free.

H.M.Jr: Four o'clock, or any time?

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Hanes: Any time after I'm through here.

H.M.Jr: Let the two of you go over there, and there's no question.

(On phone) Jesse Jones, please.

If Jesse tells everybody he wants to do something for China, let's find out where he stands.

Hanes: Ed, do you see any bugs in this thing now?

Oliphant: Now, on the ....

H.M.Jr: Do you want to take Ed with you? Take Ed with you.

Hanes: I believe I will.

H.M.Jr: Take Ed with you.

Oliphant: Now at the right moment I've got something I want to say. Want to wait until you hear from Jesse?

H.M.Jr: Goddamn it, it's always the same thing - always moving and your hands are tied. I'm saying to you, if Jesse says, "Make it three years instead of five years," I wouldn't - if that's the final stumbling block - but get him and see if he will agree in principle that we should advance six cents a pound or five cents a pound, whatever you decide - in principle - against this importation in advance. That's the thing. And will he go along?

Hanes: The reason we took five years was to get in more money, to get the maximum amount of advance.

H.M.Jr: See? I mean there's no use wasting your time with the paint and varnish industry if we ourselves won't do it.

Does that clear you up on this?

Hanes: Yes, sir.

H.M.Jr: (Nods to Oliphant)

Oliphant: We have a special section of the Antitrust Act bearing on foreign trade, and when you called up yesterday,

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wanted this thing pressed, I decided for myself I'd reached the point where I wanted to clear with the Department of Justice, carry the Department of Justice along on it, because they are responsible for that Act.

H.A.Jr: And so what?

Oliphant: I called up Thurman and he has designated a man, and I want to talk to him and I want them to go right along.

H.A.Jr: O.K.

Oliphant: Right?

H.A.Jr: All right with me. Certainly what we're talking now - there can't be anything about ...

Oliphant: Well, I want ....

H.A.Jr: Well, make awfully sure, Herman, because this thing has been - we've been talking about this thing now for weeks, see, and if we can't do this we can't do anything for the Chinese, and the sooner Chen leaves, goes home, the better for him. See? Because if there's any question - because this thing has been around now for weeks, this idea - why, we had it before Taylor went away on his vacation. I don't see why bring up the antitrust stuff now.

Oliphant: Well, if this were a question of public finance, I'd decide it myself and wouldn't ask anybody.

H.A.Jr: (On phone) Hello ...

If it was what?

Oliphant: I say if this were a question of public finance, I'd decide myself, wouldn't ask anybody.

H.A.Jr: Why didn't you bring in Justice six weeks ago on this thing?

Oliphant: Because I didn't figure we should discuss it outside of the family.

H.A.Jr: It's awful late in the thing. We've been working on the thing for weeks. And now you raise the question of

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the Department of Justice coming in on this thing.

- Foley: I don't think we'll have any trouble with the Department of Justice. Just to get them familiar with it, so they won't raise a question afterwards.
- H.M.Jr: Well, we're so deep in this thing. Why not six weeks ago?
- Oliphant: Well, as I say, I didn't feel that we could have discussed this thing.
- H.M.Jr: You could have asked me, could have said to me, "Let's ask them." We've asked the Department of Agriculture, we know where they stand. We know where the State Department stands. I mean it seems so late to have all these doubts raised now.
- Oliphant: I'm not raising any doubts.
- H.M.Jr: What?
- Oliphant: I'm not raising any doubts.
- H.M.Jr: Well, you're - I still say, though, we could have asked them six weeks ago.
- White: Do you want us to examine any other channel - other than the Export-Import Bank?
- H.M.Jr: Yes, because I don't think we're going to get this through. I don't think you're going to get it through.
- White: Might explore other possible channels of financing.
- H.M.Jr: I'm going to go through the motions. Give anybody even money that this thing will not go through. I don't think that Taylor's going to recommend it, and I don't think that the - I don't think that the form that this takes - I don't think that the State Department will.

But it certainly - we've got an awful lot of stuff to do. Let's get the thing out and finished, and let Mr. Jones take it, if he will go along, and I think he will, and say, "All right, Jesse, the Treasury Department recommends this thing, now here it is; will you please take it and see whether you can get it through," and turn it over to him. I told him whenever we got



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ready - I told him whenever we were ready we'd bring it to his attention that we're ready. I'll say, "We're ready - I wouldn't bring it over till we are ready - but first before we expose Chen to this stuff let's find out whether the Government is ready to do it."

White: Mr. Jones has already indicated to Ed Foley and myself when we were both present discussing this plan that he was agreeable.

H.M.Jr: I still don't know whether he'll go along, because he knows of all this opposition.

(On phone) Hello. - Hello, Jesse. We've gotten this question of making an advance against tung oil to the point where I'd like Taylor and Hanes to call on you at your convenience some time after four o'clock today. - Four-thirty. And they want to bring it - what I want to do is to decide whether the R.F.C. and the Treasury are ready to say, "We recommend this." See? And then if we do, then, as I said, we'll turn them over to you and ... - Thank you. (Finished)

4:30. Then it gets down - what it gets down to is to have Jones call a meeting of the directors of R.F.C., this thing will be put before them, and say, "If the Chinese are willing, will you vote this thing?" I mean - and make a vote of it.

Can you (Oliphant) have an answer by tomorrow from Justice?

Oliphant: Oh, I'll have an answer by 4:30.

H.M.Jr: What?

Oliphant: I'll have an answer by 4:30.

H.M.Jr: God! Didn't we start this before I went to Europe?

Oliphant: Yes.

H.M.Jr: What?

Oliphant: Yes.

White: Well, very tentatively before you went to Europe. Very tentatively. Had a general idea. But the issue has

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been clear since that time.

H.M.Jr: Well, I tell you, we'll make a little pool here, see - everybody drop 25 cents in - that we decide whether this thing will be accomplished or not, see? 25 cents. I'll put myself down first - H.M.Jr. And I'm going to vote for it and I'm going to do everything I can, see? I'll let you read what I wrote afterwards.

Hanes? I mean you can - bring up the 25 cents - yes or no?

Hanes: Yes, I think we can sell it if we go to work on it.

Lochhead: I'm saying yes, we can work something out.

H.M.Jr: Tung oil - just thinking of this thing.

Oliphant: Tung oil through Export-Import.

H.M.Jr: Tung oil through Export-Import.

Oliphant: That's the bet.

H.M.Jr: That's the bet.

Lochhead: I still say yes.

H.M.Jr: What?

Lochhead: I still say yes.

H.M.Jr: White?

White: I'll say no, because if I lose I'll be happy.

H.M.Jr: No, no - intellectually.

White: No intellectually.

H.M.Jr: No. All right.

White: Through the Export-Import Bank.

Foley: I say yes. I'm an optimist.

Oliphant: It won't get through.

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H.M.Jr: H.O., no.

Morgenthau, no; White, no; H.O., no; Lochhead, yes;  
Hanes, yes; Foley, yes.

Well, there's 75 to 75 cents.

Lochhead: Even money bet.

Oliphant: Archie keeps the money.

H.M.Jr: 75 cents on each side.

Lochhead: I still think we should have had odds.

H.M.Jr: Not on 25 cents.

Lochhead: I was counting on being the only boy voting yes. I  
was counting on being the only fellow for this. Turned  
out to be an even money bet.

Thursday  
October 20, 1938  
12:09 p.m.

HMJr: Hello.

Operator: Mr. Jones' extension is busy - I'm waiting for him.

12:11

HMJr: Hello.

O: Mr. Jones. Go ahead.

HMJr: Hello.

Jesse  
Jones: Hello.

HMJr: Jesse.

J: Yeah.

HMJr: We've got this question of making an advance against tung oil...

J: Yes.

HMJr: ...to the point where I'd like Taylor and Hanes to call on you at your convenience some time after four o'clock today.

J: All right. Tell them to make it four-thirty.

HMJr: Four-thirty?

J: Yeah.

HMJr: And they want to bring it and I - what I want to do is decide whether the R.F.C. and the Treasury are ready to say, "We recommend it." See?

J: All right.

HMJr: And then if we do ah - as I said - we'll turn them over to you and -

J: Tell them I'll see them at four-thirty.

HMJr: Thank you.

J: Goodbye.

Thursday  
October 20, 1938  
2:11 p.m.

HMJr: Hello.

Operator: Mayor LaGuardia. Go ahead.

HMJr: Hello.

Mayor  
LaGuardia: Hello, Mr. Secretary.

HMJr: How's the Mayor?

LaG: Feel pretty good. Say, Mr. Secretary.

HMJr: Yeah.

LaG: In trying to break down the between the  
Treasury Department and the City of New York -

HMJr: Well who's trying to do that?

LaG: Now look, ah - you know our rule on these banquets  
on the ships has been working out very well.

HMJr: The what?

LaG: This - we have - the rule that we started four -  
four and a half years ago permitting no public  
banquets on board ships.

HMJr: What kind of ships?

LaG: Ah - ocean liners.

HMJr: Oh. I thought you meant -

LaG: It was a nuisance both to your Department and to  
the City.

HMJr: Yeah.

LaG: And it's worked out well. Now we find that the ah -  
the U. S. Lines are just disregarding and breaking  
it down.

HMJr: Yeah.

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LaG: He had a dinner the other day on the ah - BRAZIL. Tonight they're having a dinner on the URUGUAY.

HMJr: Yeah.

LaG: Well now, can't you give me help on that?

HMJr: I - I - yeah, do you want - you don't the one called off tonight, do you?

LaG: Well, if you - if you'll serve notice that'll be the last one.

HMJr: I'll tell them no more.

LaG: Will you please.

HMJr: Now, let me - then - what - what were the reasons for it?

LaG: The reasons are this: first, ah - it competes with tax paying hotels -

HMJr: I see.

LaG: - that sell tax paying liquor.

HMJr: I see.

LaG: And ah - it creates always a - ah - in the old days a bootlegging problem -

HMJr: Uh huh.

LaG: And in these days always a little smuggling problem.

HMJr: I see.

LaG: And then it isn't fair to ah - to compete with the hotels - they don't carry passengers at sea and the ships in port shouldn't ah - do a hotel business here at night.

HMJr: Well now, is that Line under P. S. Franklin or is it the Maritime Commission?

LaG: It's the Maritime Commission.

HMJr: The Maritime Commission?

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LaG: Yes. All the rest are obeying and have - have been obeying for the past four years and six months.

HMJr: When here come these 'God-damned' government ships and they don't obey. What?

LaG: Yes. They're the only ones that don't.

HMJr: Well, what do you know about that?

LaG: And they <sup>if</sup> -/ they defy us - I'll have to break the lease and ah - it just shouldn't be done by a government agency.

HMJr: Ah - I'll promise you that this is the last one. I think if - to call it off now would look kind of bad, don't you think so?

LaG: Yes. Well, the ah - the ah - Dock Commissioner has served notice that it's in violation of the lease.

HMJr: Yeah.

LaG: And ah - but if you - if you'll help me I'll be very grateful -

HMJr: I'll - if you -

LaG: - because it's a relief both to your Customs and - and to the City Police.

HMJr: What's the name of the boat tonight?

LaG: URUGUAY.

HMJr: URUGUAY. Ah - if you don't hear from me <sup>in</sup> /the next hour -

LaG: Yes.

HMJr: - you'll know that this is the last one that's going to be held.

LaG: All right. Thank you.

HMJr: How's that?

LaG: Thank you so much.

HMJr: Hope to see you soon.



Thursday  
October 20, 1938  
2:15 p.m.

HMJr: Hello.

Operator: Admiral Land is away until November 3rd. His secretary is on the wire.

HMJr: Well let me talk to him.

O: All right.

HMJr: Man or woman?

O: Woman.

HMJr: All right.

O: Secretary Morgenthau.

HMJr: Hello.

Miss Eleanor Van Valey: Yes, Mr. McIntyre.

HMJr: Who is this, please?

V: Miss Van Valey.

HMJr: Now, look -

V: Uh huh.

HMJr: I wonder if you can take care of me.

V: I'll try.

HMJr: Mayor LaGuardia just called up.

V: Yes.

HMJr: And for four and a half years they've had a rule - no banquets on any ships docked in New York.

V: Uh huh.

HMJr: And for the first time -

V: Look - I - let me tell - let me interrupt you on that.

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HMJr: Yes.

V: He called Admiral Land on that first ship.

HMJr: Yes.

V: And Admiral Land told him that it wasn't a matter of competition at all - this is a Government affair and it isn't going to be a - a rule or anything like that and he - ah -

HMJr: I know.

V: He was perfectly satisfied about it.

HMJr: Well he's not now and he's going to cancel your lease on your dock unless this is the last one.

V: Unless this is the last one?

HMJr: On the URUGUAY. If it happens again he'll cancel your lease.

V: (Laughs)

HMJr: Well he's in - he's serious.

V: Yes. I know it. He was serious but when Admiral explained to him it was the Government -

HMJr: No. No. he's - this is the last time and if there's another one held the lease is going to be cancelled. Now I want - you'd better take it up with the Commission. -

V: I will.

HMJr: And let me know, because ah - if there's any question I'll - ah - there's a Customs law involved in it too.

V: Yes. Uh huh. All right. I'll take care of it.

HMJr: But he's very serious and he says if it happens again he's - he's already - the Dock Commissioner served notice. -

V: Uh huh.

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HMJr: And he's going to cancel your dock permit.

V: Uh huh. I see. Well, I don't know off hand what - there's only one more and whether they plan that or not -

HMJr: Well, they'd better not.

V: But we'll not - we'll take care of it.

HMJr: Well, they'd better not.

V: All right, I'll take it up, and take care -

HMJr: But, whoever is the boss over there -

V: Yes.

HMJr: - besides yourself.

V: Yes. (Laughs)

HMJr: Ah - let them - let me know, will you?

V: I'll take care of it, yes.

HMJr: Because I told the Mayor that if there was any argument about it I'd call him back.

V: All right. Well, I'm sure there won't be.

HMJr: Thank you.

V: And I'll take care of it.

HMJr: But he's not going to stop this one tonight but if -

V: He's going -

HMJr: If there's any more -

V: Uh huh.

HMJr: He'll cancel your lease.

V: All right. I'll take care of it.

HMJr: And he goes through with it too, you know.

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V: Yeah, I'm afraid he would.

HMJr: Right.

V: All right.

HMJr: Thank you.

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## NATIONAL RESOURCES MEETING

October 20, 1938.  
2:15 p.m.

Present: Mr. Hanes  
Mr. Taylor  
Mr. Bell  
Mr. McReynolds  
Mr. Eccles  
Mr. Haas  
Mr. Frederic Delano  
Mr. Beardasley Ruml

H.M.Jr: Well, gentlemen, we're meeting today at the suggestion of Mr. Delano, and I just want to say this - just one little thing kind of bothers me a bit, and I'm going to be perfectly frank. We've always been able to keep budget figures absolutely secret until they went up in a budget message, and I would feel just sick if information as to the budget figures should get out, and I'm just going to ask all of you as gentlemen to give me your word; and that it cannot be passed on to your associates, and you're here as individuals, because this is property belonging to the President of the United States. And as I say, the four years I've been here we've never had a leak, and I'm more than pleased to sit down - Mr. Bell is - get your advice and your ideas, and we're going to tell you the whole story. But I must ask you to treat this as property of the President, and as such it must be absolutely secret, and I think that's enough. But we were bothered a little bit about our legal right to disclose this information; but we've satisfied ourselves, we think we can. You bothered about that, Marriner?

Eccles: No, that doesn't bother me any. I would have no occasion to use the figures one way or the other.

H.M.Jr: Well, I'm just making - I'm going to say it's - I mean they had a national scandal in England over a leak on the budget; I don't want any while I sit in this chair. So if you can treat it as individuals, I'm confident there won't be any .... So with that little introductory remark, I'll turn the class over to Professor Bell.

Bell: Well, these are the figures that were presented to the President last week, and the figures so far as 1940 is concerned - we haven't yet gotten to the point where we can say how much each department is going to get in the way of appropriations.

You recall that the budget summation which was issued

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in July showed estimated receipts for 1939 of five billion dollars and total expenditures of eight billion 985 million, and a deficit of three billion 985. Now, of those total expenditures, there is approximately five billion 900 million of the regular departmental, including Social Security, CCC. WPA was two billion one, and other emergency expenditures 900 million.

Now the picture for 1940 - tentative estimates that we've gotten from the Treasury for receipts - shows four billion 850 million, a drop of about 150 million dollars, and it looks as though the expenditures on regular account are going to be about six billion 600 million, increase of about 650 million dollars over 1939; and other emergency expenditures, which means nothing more than a backlog that's carried over from '39 into '40, of about 800 million - coming out with total expenditures of seven billion 426 million. That leaves a deficit of two billion 576 million. When the President saw those figures he immediately added a billion and a half for WPA and said, "Of course, that's as little as we can get by with," in his opinion, making a deficit for 1940 of about four billion dollars, slightly higher than the 1939 deficit.

That's about the picture as to the budget. Don't know whether we can get any further.

H. A. Jr: Why not let them ask you questions? - - Go ahead, Eccles, don't you want to ask some questions?

Eccles: Well, as you know, this thing is all somewhat new to me, and I had somewhat conceived of the work of the Committee in a little different aspect than merely the question of considering a budget as such. It seems to me the important thing we've got to consider is the importance of fiscal policy as a means toward the maintenance of economic stability.

Now, we have - I have always thought of a - what I term a compensatory fiscal policy; that is, a fiscal policy that is compensating in its relationship with private business activity; that the question of public expenditure has to have some relationship to the private expenditures, and it's a question of timing, it's a question of taxation and the form of taxation.

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It seems to me that fiscal policy, instead of being merely a means of collecting revenue and disbursing it, occupies a more - the most important place as a mechanism for stability. There isn't anything, in my opinion, that - monetary is certainly secondary, very secondary, in relationship to fiscal.

Now that's just a broad statement of my approach, and I was interested in it from that standpoint rather than this. The question here is on the budget; what effect will a budget as is proposed here, we'll say, have upon the economy as a whole? Will it be inflationary? Should there be a deficit of that size, or should that deficit be reduced by an increase of taxation, and if so, what kind of taxes should reduce it? Or should expenditures be reduced? Is the budget being considered from the standpoint as to what effect its application will have upon the stability of the economy, looking to the future when it is applied?

For instance, we go back to '36, and in '36, of course, there was a very large deficit due to the bonus. It gave a real stimulation to consumer buying power, because it - the Government contributed the difference between the cash that it received and the cash that it expended. That difference was its contribution to the whole consumer buying power, and it had an inflationary effect, there was no question; whereas in the next year, with the bonus not being paid in '37 - I'm speaking of the calendar year - and the Social Security taxes being collected, which they were not collected in '36, there was a difference, as I recall the figures, of something like a little over three billion dollars: difference between the Government's contribution to community buying power in the years '37 and '36. It was inflationary in '36 and deflationary in '37. In other words, in '37 the Government contributed the difference between their expenditures and receipts - in '37 was about 400 million; in '36 was about three billion 600 million. They actually contributed over three billion less in '37 than they did in '36. Well, it was deflationary.

So that if there is a mechanism within a democracy that can act as a - in a compensatory manner and in a functional - this can operate in a functional and a compensatory manner to maintain stability, it is in the fiscal



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operation of the Government.

And I don't think that I can contribute anything toward a solution or - with reference to the matter of advising on - on just - you take those figures; it gives the budget of so much. Well now - and it gives a deficit of so much. The question is where those expenditures are being made. In making expenditures, are they tending to create an unstable situation, an inflationary development in certain directions? If expenditures as provided are made, should they be financed by borrowing, by deficits, or should they be partly compensated or supplied by borrowing and partly by taxation?

Bell: It seems to me that's the question.

Eccles: <sup>the</sup> That's/thing.

Bell: What we're doing is telling you that we're faced with a deficit in 1940 of four billion dollars, on top of a four billion dollar deficit in 1939. Now, now are we going to handle it? Are we going to finance it through continued borrowing or are we going to have some more taxes to take care of it, or are we going to reduce expenditures? It seems to me that's what the Secretary - speaking for you (H.M.Jr), that's the advice you want, how to handle it.

Eccles: That's right. After all, that ....

Bell: That's the question.

Eccles: Well, I - I think, of course, that involves certainly a study of the problem. I don't think anybody could arbitrarily say that a deficit of that size would be inflationary or disastrous. It depends a good deal upon what the national income may be. I think that a budget has got to have some flexibility.

Bell: It has.

Eccles: Of course, the relief expenditure is - can be used in a flexible manner. It can be increased rapidly or decreased rapidly, can't it? That's the one element of the budget that has flexibility.

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Bell: It can be increased. I don't know about ....

Eccles: It could actually be decreased if you had a condition of shortage of help, for instance, and business activity absorbing ....

Bell: With a boom it would go the other way.

Eccles: You could pull it in.

I'd like to hear what Mr. Delano and Mr. Ruml have to say. That's my general conception of the thing.

Delano: Mr. Secretary, I think my colleague, Mr. Ruml, knows a good deal more about the subject than I do. I think I am as eager to see the budget balanced as any citizen, but I have made up my mind that we're not talking simply of balancing the budget in money, but we're talking about balancing the budget in goods and services and all that goes with it.

I have here, for instance, in my hand something which was handed to me only yesterday, showing the construction work of the country the last twenty or thirty years. In the years running along from '25 to '26, '27, '28, '29, we were running close on our gross construction estimates to 14 billions a year. And we dropped from that peak suddenly down to four billions in the year '33. The public works, non-federal, which had been going on a pretty high scale, over three billions a year, largely on borrowed money, suddenly squeezed down to about a billion and a quarter. The public utilities, which had been going along on an expenditure of about two and a half to three billions, squeezed down to about one billion. The non-residential budget, which had been going along on about three billions, squeezed down to about one and a half; and the private construction, residential, which had been going perfectly high, wide and handsome at about three billion, squeezed down also to almost nothing. And it left the Federal Government to carry the whole load, and it was a terrific load, and in spite of all our - all we have been doing, we haven't been able to take up the slack.

Although we have managed to increase our - I don't know how low our national income went in that worst year, but perhaps 30 or 40 billions - we have been

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able to pretty nearly double that, but we can't get back to times such as our people apparently are accustomed to and want to see, which will require a total national income of something like 85 billion - we can't get that going unless some of these other departments of our population can help carry the load.

People talk a great deal about mounting national debt. But perhaps national debt properly viewed, if by national debt we mean, as we do in the case of national income, the aggregate debt of all contributing populations - probably the national debt has decreased in the last four or five years. I don't have the figures on that.

But the way I view this suggestion of the compensatory budget that Mr. Eccles talks about, which I believe in almost as a sine qua non - it isn't because I want it; I believe in it because I think you've got to have something to take up the slack which the other departments of government, that is, state and municipal, and private industry, semi-public utilities, and finally private spending, won't take up or can't take up.

H.M. Jr:

Mr. Ruml?

Ruml:

Well, I suppose the interest of the Resources Committee in fiscal policy springs from the assumption that Mr. Eccles has just made, that what the fiscal policy of the Government is, that is, whether it is making a net addition or a net subtraction from purchasing power, has a very vital relation to the conservation of national resources both physical and human.

We have made estimates, but as of the year 1936, that without any extraordinary pulling of rabbits out of a hat we can produce about 88½ billion dollars worth of income. We estimate roughly that between 1929 and 1936 we lost about 200 billion dollars worth of production; that is, production that's gone forever, because the one resource you can't conserve is labor that isn't used.

Now, has the system been working right? There's lots of things that make it wrong. That 200 billion dollars in goods and services would have been used for individual and public betterment, and that wealth would have been created.

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Although we haven't got the figures now, I suspect that that figure is now nearer 92 or 93 billion dollars today - this is at the 1936 price level - than 88 billion, because there's been obviously some important technical improvements in the last three years.

H.M.Jr: I don't understand - 90-odd billion of what, Mr. Ruml?

Ruml: Potential national production.

H.M.Jr: That's separate from national income.

Ruml: quite. About 50 percent difference, Mr. Secretary, at the present time.

Now, from the standpoint of getting the most out of the country for the country, it seems important that we should attain that production as it becomes practical to attain it. And therefore I think that the interest that we have in fiscal policy comes from an attempt to, as I say - to conserve production, conserve human resources. Now therefore, any comment on the budget that Mr. Bell proposes from our point of view would be in terms of the extent to which that forwards the general objective that we have in mind. And it is difficult to know, in the absence of estimates as to what the national income is likely to be, independent of budgetary operation, what the effect of this is likely to be.

And it is as Mr. Eccles points out: you can't attain your objective simply by arithmetic. There are going to be plenty of bottlenecks and special situations that are going to make it impossible to make progress overnight.

H.M.Jr: Well now, just to break in on your thought a minute, let Mr. Haas show you some very interesting figures which we have, taking national income and stepping it up: what it means if national income is a hundred million and what - on the present tax basis, what it would produce. I think if he'd show you that - I think it would show you ... Then we'll come back to the point that you people are talking about.

Well, in order to balance the budget, his figures show we need an income of a hundred million.

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Bell: Billion.

H.M.Jr: What?

Bell: Billion.

H.M.Jr: What is it, billion? I've just been on the farm. I can't think - been thinking in terms of selling a bushel of Mackintoshes, and I'm a little bit mixed up.

But he's got - Dan and the rest of us have seen it. Bring it over here. And then if those three gentlemen who are visiting would look over your (Haas) shoulder .... Murriner, I don't think you've seen it.

McCles: No, I haven't seen it. This is the estimated revenue based on present taxes if the national income goes to a hundred?

Haas: Different levels.

H.M.Jr: Different levels. Your Federal Reserve index and the price level. The thing that interests me particularly is that if your Federal Reserve index goes to 149, your price level only goes to 100. You explain it, George.

Haas: Here is a level of 60 billion dollars national income. At that level, assuming the present tax statute, we estimate that the receipts will be four billion 992 million, and here's the breakdown of it. And here's the same thing for a level ... And here, to show you - to give you some idea of the composition of it, is the FRB index, in '38, 82, and price level 80. That's about correct.

Then this next column here shows the same thing for a level of 70 billion dollars of national income. Our present tax structure would yield six billion 703 million. And we give you some idea whether we're assuming an inflation or price rise - 85, slow price rise, 108 FRB index.

Here's the same thing for 80 billion dollars. You get eight billion 451 million dollars in revenue, and Federal Reserve index of production 123, price level 90.

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And here's the same thing for 90 billion dollars. You get 10 billion, 96 million - and the income tax so much, internal revenue so much; and the Federal Reserve Board production index 137 and the price level 95. And here's the same thing for 100 billion dollars. You get 12 billion 348, and FRB index 149, price level 100. Down here is the percentage distribution.

Now, these are - these are rough estimates, but they are approximately right.

Ruml: This is the wholesale prices.

Haas: That's right.

Ruml: Do you happen to remember what that was in 1936? Was it about that figure?

Haas: About 78 now. It was a little higher than that. I haven't the Bureau of Labor - I don't have that sheet.

Ruml: The reason I'm asking - I was trying to translate our 88 billion dollar figure at that price level to this price level, see whether that would be reasonable for production; because if the price level is going up, my guess is, see, that ....

Haas: That isn't far off.

Ruml: 20 percent off - that would give you about an 82 billion dollar production on a 106 price level. Isn't it ...

Haas: That's right.

Delano: Go back to 1929 and these figures are not far off - total, say, 79 billion.

Hanes: These other indices were approximately the same.

Ruml: Well then, if - this figure is certainly physically possible; that would be nearly 10 billion dollars production short of what is presumably attainable, of what physical production is possible.

Eccles: At that price level.

Ruml: At that price level.

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- H.M.Jr: In other words, gentlemen, if you can show us how to get 100 billion dollars worth of income, this thing is .... (words drowned in burst of laughter).
- Eccles: I think if that happened you wouldn't go at all; you'd be right here for life. Isn't that right?
- H.M.Jr: I'm just showing you this to let you know we're conscious of it. I want to show you one other thing - I don't want to hurry you - if you've got that picture. Any questions, Mr. Delano?
- Delano: Beautiful. Beautiful illustration.
- H.M.Jr: Now, there's no reason that, as far as that chart is concerned - be glad to furnish a copy to the National Resources Board and one to Federal Reserve. It has nothing ....
- Eccles: That's a theoretical, hypothetical case here. It isn't ...
- Hanes: It's hypothetical from here on, but this up to here ....
- Ruml: To see whether physically ....
- H.M.Jr: Will you explain to George what you want?
- Raas: As soon as I've finished this check on our assumptions...
- H.M.Jr: Then if you would have your crowd check it, and if Eccles wants to turn it over to Goldenweiser, I'd be delighted to have your ....
- Ruml: The crucial problem is whether it's physically possible to produce that amount of stuff.
- H.M.Jr: This is what we need, gentlemen. Now, if you can show us - or, first place, those things are fairly accurate, and then that's our objective. Now what I take it we talk is, we don't want to know how to bring that about - at least to give us credit that we know what we mean, see? And I'd be more than pleased to furnish each of you people with a set of those, and then any additional thing that you want on that, or using that as a base.
- Eccles: If additional questions arise, use that as a base to

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increase ....

H.M.Jr: If you just talk to George, he'll be more than pleased to.... That's an all-summer job, and I think it's a very nice one.

George, show them what I call my trial balloon chart. I've got a trial balloon chart.

Haas: The Secretary asked us to make this up for several reasons. One of them is that he wanted to know which direction the spending is going - some of the problems you (McCles) raised.

Now, these - better start here with the expenditures. These so-called balloons are the last July ...

H.M.Jr: ...estimates.

Haas: Mr. Bell asked each Government agency to submit an estimate to him, how much they were going to spend each month all the way through the present fiscal year, and each month they revise these estimates on through. So what you see here is the October estimates, these out in here. And that's the - I'll show you afterwards the breakdown by agencies, but this is open expenditures of the Federal Government, not on a budget basis; includes all expenditures of the Government, whether extra-budget or not - every agency; this is cash.

Now this line through here is a 12-month moving average centered - we're going to extend this on beyond the present time, because we have these estimates to use as figures.

H.M.Jr: You see why I call it trial balloon.

Haas: This is the July figure. Isn't it? No, I guess that's the July estimates, which are right on the head, because they're made in July. Then the next one expenditures didn't meet, and the next one was right on there. Down here was income, receipts. We find that it - well, this one was right on, and this one was somewhat over. As it works out, the receipts are running five percent ahead of the estimates and these are seven percent under.



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Now, up here you get the result of the play of both receipts and expenditures in terms of - this is a net Government cash deficit; no corrections or anything, just cash. And you will notice down here, this period you were talking about in '37, the budget was balanced on a cash basis, you see, and then from about November the spending started up. So you're starting up at a very - at quite a rapid rate, provided these estimates hold up.

Eccles: That's the estimates of both receipts and expenditures.

Haas: That's right.

H.M.Jr: Below the thing - one is receipts and the other is expenditure.

Eccles: But this is the net.

Bell: The net between them.

Eccles: This will hold up if that holds up in accordance with the estimates.

Bell: If the estimates below there are right, this has got to be right.

Ruml: If you take any point on this line, what is it an average of?

Haas: Six months that way and six months that way. What it means is that's going at an annual rate - that amount.

Ruml: Just wondered whether it's centered.

Haas: And we're able to extend it beyond the current period because we have estimates for the whole fiscal year.

Ruml: Have you made any estimates which would show in terms of what the effect of that cash deficit is on national income how many times it turns over? Would it turn once, twice, three times, four times?

Haas: I don't know.

Eccles: Wait a minute - what's that question again?

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- Ruml: I was wondering what the effective power of these deficits is, because if they turn four times they're a darn sight more effective than if they turn twice or three.
- Haas: To get some idea of that, we'd have to examine two things: where you got your money from and ...
- Eccles: He's just talking about ...
- Ruml: Just a gross average. I've seen in some economic writings the general figure of three being taken as the multiple.
- Eccles: As I understand it, what you're talking about is, if the national income, for instance, increased from 60 to 70 billion within a year and if the Government's cash deficit within that year was three billion and a half, then you could say that there was a direct and an indirect effect....
- Ruml: Exactly, that's what I mean.
- Eccles: ... from that expenditure. On the other hand, if the Government had a deficit of three billion and the national income didn't increase but three, there would be no ...
- Haas: But there are so many other factors.
- Eccles: I don't think you can figure it exactly, no, except it would be interesting always to know what happens to the national income in its upward or downward swings in relationship to the cash deficit.
- Haas: You could work out here a ratio from the increase - in this to the increase of your national income.
- Eccles: For instance, in '36, you'd say the national income went down - that's in '37 - and the public - the deficit - the cash deficit also went down very rapidly. The question is, did the income drop as rapidly, or is there a relationship?
- Haas: I think it's an accumulative relationship, not a timed one that - we've worked on it; we couldn't get the thing.

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- Ruml: We know this would be true, don't we? If there was no destruction of public confidence as a result of the deficit, if you spent a billion dollars you'd add a billion dollars at least.
- Haas: Other beings being equal.
- Ruml: If you don't have any destruction of public confidence, then you know that, taken over a year's period, certainly the amount you spend in January certainly is not going to remain in the hands of the people who got it; so it must have turned at least twice, and if it turns - I mean the least it could turn would be twice. And the question is, how much would it turn? If the darn thing turned four times, why, you've got a very different problem than if it turned three times.
- H.M.Jr: Dan, on that stuff - can we let that out, do you think? Would it be of any use to you (Ruml)?
- Ruml: His checks so closely with Federal Reserve Board estimates that the logic is just the same.
- Haas: The logic is just the same.
- H.M.Jr: The other thing we'd be glad to give you, but this ....
- Bell: Those are department estimates, and they're always high.
- H.M.Jr: R.F.C. - there's the model child.
- eccles: It always has been.
- H.M.Jr: The great deceiver - R.F.C. It's wonderful. We point with pride to R.F.C.
- Haas: This is a breakdown of cash expenditures by agencies - not a complete one. But here's the Works Progress Administration; there's the estimate in July, with these orange dots here. Well, in July - here's July - he met it. August, it's a little above. And now he's way above.
- I haven't - I just noticed that some of this is on the wrong chart. I mean this one is not the last one.

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- H.M.Jr: Why don't you send for it? Use my phone.
- Eccles: This is the flexible ....
- H.M.Jr: It always has been.
- Eccles: He's got to do it when the other fellow doesn't do it; that's natural.
- H.M.Jr: That's why one of these charts is the so-called balloon chart.
- Haas: (On phone) Second one is not the last one, not the October chart. Could you find one right away and send it on in here? Ask Sidney. Maybe Mr. Bell has a copy upstairs.
- Well, this will serve to illustrate it. Well, here - this other is all public works. The largest item is PWA. But you notice here, here's where the - where they're expecting a very sharp increase but didn't get it. Too optimistic in their estimates.
- Eccles: Misses in here, then he passed it in here.
- Bell: accumulates it and passes it on to the next month.
- Haas: That's not only one agency, but a group of agencies.
- Bell: But PWA is the one large, big item.
- Haas: Now here's the agricultural aid, including the Agricultural Acts and also the Commodity Credit Corporation. They've been falling below there. One month they were above their estimates. That was a carryover from the other fiscal year. The last month they were right on the ....
- Here's the Reconstruction Finance Corporation. He estimates he was going to take in, net, that amount, but he did a little better.
- Eccles: Twice as good.
- Bell: Well, look at the - his next month.
- Haas: Next month he said he was going to spend, but he took in five; so that made it difficult for the statisticians

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to calculate his percentage of error.

Bell: One hundred percent wrong.

Haas: Don't know what to base it on - over a hundred percent.

This is national defense, which is running along pretty regularly.

This is these trust accounts. The largest is unemployment, Dan, isn't it?

Bell: Yes.

Haas: And we've separated interest out, so there's nothing that confuses that. That runs along very regularly.

These are regular departmental expenditures, except over here it includes the bonus. That gives - that has bearing on the point you (Eccles) raise - I mean the different classes of expenditure and the effect thereof in stimulating it.

Eccles: That's very important: whether they're going to stimulate the capital goods or the consumer goods. As you get into these blooming bottlenecks, if you get all the capital goods coming at one point, such as your public works and your armament expenditures, ...

Bell: All out there in June.

Eccles: ... the whole thing coming up at one point - and then up goes your steel prices and ...

H.M.Jr: I don't want to digress, but Haas has just developed a very interesting new chart showing, contrary to '33, that the consumer goods and the heavy industry goods are moving forward together at an equal rate. Would you like that?

Delano: Yes.

H.M.Jr: Send for that, George, because that's something ....

Haas: Yes.

H.M.Jr: It has nothing particular to do with this, but it's

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interesting.

- Haas: (On phone) 630. This is Mr. Haas. Would you send me in a copy of the charts which are - which were attached to the last business statement? Right away to the Secretary's office. - O.K.
- H.M.Jr: Well, gentlemen, you see what we do here. I'll be very frank; we can tell, oh, maybe six months ahead about how the money is going out. Is that about as far as we can go?
- Bell: That certainly is as far - say, three months is better.
- H.M.Jr: Well, we can do a pretty good job.
- Well - now in this thing, for instance, there isn't the estimate of what United States Housing is going to do. I mean we haven't included that, which - Mr. Straus is right, we're going very big after the first of January. In other words, non-budgetary expenditures, but which are fostered by the Government.
- Of course, talking about national income and what the Government can do, I think those non-budgetary items should be in there, and I think they should be more and more important. Now ..
- Eccles: The Federal - United States Housing should - if that involves the Government financing of that almost entirely, that does affect your budget - the FHA ....
- H.M.Jr: No, they don't affect my budget.
- Bell: You mean the United States Housing Authority. They get their own money, guaranteed.
- H.M.Jr: The only thing it costs - 30 or 35 million dollars, interest contribution.
- Bell: 28 million is the maximum subsidy.
- H.M.Jr: If they ever get going, the direct contribution is very small compared to what he will do if he's spending a hundred million dollars. I mean I think we ought to study those particular things and also that possibility - whether they can be developed.

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Eccles: That's right, because they have the same effect on the national economy as though they were direct Government expenditures.

H.M.Jr: I think they're important. But here in the Treasury - I'm talking of us (Bell and H.M.Jr) together - what we can do is - I mean we can show you this.

Now, of course, there's always the other factors. Unfortunately - we're talking here in this room - there is - our work with WPA is always on a 24-hour basis. I mean they're never worth much more. That may be a slight exaggeration. But certainly the last week we had a demonstration. On Tuesday they gave us figures saying they were going to be out of money on the first of February; then they saw the President and the paper carried a statement that it would last them to the first of March. Just using that as an illustration.

And what our thing is, as far as - as much as anybody, is to get all of this together, so we can look forward. What we've got to do now, between now and January, is look forward 18 months. We've got to give the President an estimate of 18 months beginning in December, which is effective until the fiscal year beginning July 1, 1939. We can say, "Well now, four billion dollar deficit is or isn't - nine billion dollars is too much or too little." But being a conservative fellow, this four billion dollar deficit on top of another four billion dollar deficit naturally scares me, and I think it would scare any business man, because we're going into the unexplored realm. Maybe we can do it; I don't know.

But if we had information to back us up to show what we could do to get this income up to 100 million dollars - that's where I'd like to see it - and take everything into account, and particularly explore the realm of the non-budgetary items such as - United States Housing is the best example I know of. And after all, if they spend 800 million dollars, it isn't necessary maybe for Ickes to spend quite so much, and it doesn't come in the budget. And there's the thing.

And then, I haven't given Hanes a chance, but if you want to turn your stomach upside down, he can tell you

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what it's necessary to do when we go beyond the five billion dollar tax program. And just give them a little shock.

Bell: Before they leave that chart ....

H.M.Jr: I mean tell them what we've got to do when you talk about going above a five billion dollar tax program on the present level of business; on the present level of national income, what it means to raise above five billion dollars.

Bell: I just wanted to say, before they leave that over-all chart, you ought to be interested in seeing the last line - the estimates of the last month on there; think it goes over a billion dollars, at which rate expenditures of the Federal Government are on a 12 billion dollar annual basis; means to meet that, if it is more or less of a permanent thing, you've got to get 12 billion dollars revenue, which means 100 billion dollars national income.

H.M.Jr: You mean month of June.

Bell: Yes, sir.

Ruml: But if you have the turnover that you want, you're producing a national income ...

Bell: It doesn't work that ...

H.M.Jr: Think about that for next meeting. I think it would be grand ...

Ruml: I think we can get preliminary shots - different things can have different effects.

H.M.Jr: If you can develop that going back and then also going forward, as to what that means - I mean the normal thing is, we sit around here - I'm being very frank - "Oh my God, what a headache, I'm facing another four billion deficit." Then I get a weak stomach and then Mr. Hanes comes along, just to make sure that I'm thoroughly upset, and tells me what it means on the present national income to raise above five billion dollars. It's damn near impossible.

Now, Johnny, give them the works.



Hanes:

I think we'd like some words of wisdom from all the people we can get it from as to where we're going to turn to get this revenue.

First of all, going back to Mr. Eccles' term, the flexibility of the budget, and that part of the budget which is flexible, we are considering seven and a half billion, as Danry Bell's pointed out, as what we call for a moment the inflexible budget. That leaves us with, roughly, a two and a half billion dollar deficit before we do any extraordinary spending at all.

That brings up the problem as to how we're going to meet this deficit. Shall we do deficit financing, hoping to increase the income - waiting to increase the income, or are we going to meet the problem with a direct attack upon it by way of raising revenue to pay the cost of government as we go?

That raises three questions which I'd like to hear discussed, which we're studying very carefully. One: to what extent should the taxes be raised? Two: from what sources should those increases come? And three: should the increase in taxing people be effected all at once, or should it be distributed over more than one year, and if so, how many years? What way should we attack that problem?

If you start out and say we're going to raise two billion dollars, or two and a half billion dollars, or three billion dollars in additional taxes, then the first question comes, are you going to raise it immediately, are you going to impose those rates which would be sufficient to bring it up to that in 1940, '41, '42, '43, or when?

If you're talking in terms of two billion dollars or three billion dollars, in order to raise that much there are just a few sources from which that revenue can be raised. One: the income tax. Two: the corporation tax. Three: the estate and gift tax. And when you reach that limit you've about exhausted the possibilities of any large increase from existing revenues other than a few minor ones, such as ... You might consider the liquor tax. Some think the liquor tax is probably high enough. Be that as it may, you've got tobacco revenue, you've got a stamp tax. But we're dealing there in terms of 40 and 50 million dollars

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revenue, whereas we're considering two and three billion dollars revenue. So those things, those items, don't add up.

So if you attack the problem, it comes down to a final analysis which just leaves you about three places, without going into some new kind of tax, some new source of revenue, which I'm not discussing now, but just the known and existing sources of revenue. That means an increase in the number of people paying income tax upwards of eight million. That means a lowering of the exemptions from twenty-five hundred to two thousand, from one thousand unmarried to eight hundred, which would bring about a million 600 thousand people in under the income tax, and the enormous increase of those incomes all the way from a thousand dollars net - not a thousand dollars total income, but a thousand dollars net taxable income, which means at the minimum \$2,777 yearly; that means taxing those incomes at a rate of more than 100 percent more than now is being raised.

Well now, all those questions are questions which we are exploring and which we, I think, would like to hear some opinions on. I certainly would. There's the problem; we've got the problem. Easy enough to state the problem. We've got a five billion dollar income and we've got a nine billion dollar outgo.

Ruml:

Well, Mr. Hanes' problem makes me think of Macy's, Mr. Secretary, in one respect, on the assumption that if you get an insufficient national income he's got a terrific problem of trying to get even. I had to make some computations as to how Macy's could make a profit out of 75 million dollars income; we'd been running at 90, and things didn't look so good last spring; and we found out it just couldn't be done. And therefore, what we had to do was to get our volume, even though it might be expensive, which we proceeded to do.

In other words, if you've got a lot of fixed expenses, the only way you can be in the black is to have a volume that's big enough to take care of it. As far as I can see, that's the only ....

Hanes:

Of course, you have ....

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Ruml: That doesn't solve your problem.

Hanes: It would solve it, of course, if we would attack this problem as you have attacked it, where you're going out of business if you don't solve it.

Ruml: We have to get the volume.

Hanes: You have to get the volume. It seems to me we're confronted with a business proposition which is, in simple terms, that we've got to get our economy going on all fours or we are not going to collect the revenue.

Ruml: Well, that's the business answer.

Hanes: It seems to me the source of all of our difficulty and what I've been hollering about for six months at least is that our economic machine is not functioning, and that if we all bend our efforts - we're trying to spend this money - but trying to fix this machine which is not producing: there's where we're falling down, in my opinion, in government today. There's only three possible ways to get out of this: increase taxes, reduce expenditures, or build up the national income.

Ruml: Of course, it may not be "either ....or." Maybe we can do some of both.

Hanes: I think you've got to do a lot of both. I agree with you. You've got to do a lot of both.

Eccles: Well then, if ....

Hanes: Excuse me.

Eccles: Go ahead.

Hanes: I was just going to - bringing it down to the question here which is puzzling all of us, I think, and - as to what recommendation are we going to make as to a method of closing this gap.

Ruml: Let me ask you this question, Mr. Hanes. Have you made any estimates of at what level of national income private enterprise would go ahead?

Hanes: No, I don't think anybody here has made any such estimates.

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- Ruml: Because it was perfectly clear that the 1937 - 70 billion - there was plenty of capacity to take care of that income without any substantial new investments. We saw that thing in Macy's very clearly. Had we had another five percent volume, we would have had to build a warehouse.
- H.M.Jr: You would not?
- Ruml: We would have. We were just at the edge of the position of having to make an investment, but we didn't have to, and we're getting along very well now, thank you, without having to make any, and we won't have to make any without getting to 90 or 95 million dollars. Now, I'm not comparing Macy's with this problem. But there must be some point - probably some point between 72 and 80 - before you can expect any substantial private investment.
- Eccles: Outside of the maintenance of the existing facilities. You've got that.
- Ruml: Your depreciation account washes that sort of thing, but you won't get new investment until you get demand.
- Eccles: That's an expenditure, if they'll expend the depreciation account instead of accumulating, which they do. The first thing they'll do as things begin to turn up, of course, is maintain plant facilities; when it goes beyond that, until the capacity is adequate - and I agree with you that the national income has got to get higher than it has been since the depression before there is going to be any real justification, taking the thing as a whole - there are isolated cases, but taking the thing as a whole, before there will be any real normal private expenditure in new facilities. And then these people can talk about just having confidence, and they'll go ahead and do these things. It just doesn't make sense.
- Hanes: You might translate that back into a form - it gets historical - which would be permanent, which is this. In a period, say, 1924 to 1930 - to compare the national income of that period with the expenditures of private capital, and just take in that - not the refinancing issues, but just take the pure injection of new money into the economy. And then in that period you find you

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had about 450 million dollars a month....

Ruml: Sure.

Hanes: ...injected into the economy, which had some relationship, undoubtedly, to what you were talking about; that is, the national income.

Ruml: Sure.

Hanes: Now, your question is, how much of that injection was producing overproduction, and how far will we have to go before that overproduction is worked out, and then from that point on we'll begin to expand, with private capital coming back on again.

Ruml: It doesn't make a particle of difference whether the purchasing power is created by private industry or public borrowing; functionally it's the same thing. But you've got such an increase of efficiency that your point of demanding new capital is probably much higher than it was in the '20's.

Taylor: Have you got any figures on the Board, Mr. Delano, that would bear on the ....

H.M.Jr: Have you (Haas) been making notes?

Haas: No, but I meant to.

H.M.Jr: Well, I think the thing to do afterwards is, if Mr. Ruml can stay behind - maybe you're going back tonight?

Ruml: I'm staying here.

H.M.Jr: You and George Haas can get together. Let's check up what we need and where we'll go to get it, until next week.

Ruml: Fine.

H.M.Jr: You stay behind.

Ruml: I'll be delighted to.

H.M.Jr: So at the next meeting we can have that. And if we haven't got it - we have no pride - we'll beg or ask anybody else for it.

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Ruml: I don't feel particularly competent, but some of the ....

H.M.Jr: Well, between them there - we know at least where we can get the thing.

But I agree with Hanes; if we could get to thinking here in this Administration - instead of always worrying about deficit or taxes, if we could get the Administration's thought channelized around how we can all do everything to raise the national income, why, my job might be a little fun for the year that I was here. And I mean if everybody would start to think, what could we do to get the public utilities to spend, what could we do to get the railroads to spend, what could we do on this, that and the other thing - but to handle it all. That kind of thinking - well, if it's going on, it's going on in individual brains, it isn't going on in groups; if it is, I don't know where it is, because I haven't run across it.

Ruml: It's all part of what's going to be the fiscal policy.

Eccles: That's right. That's right.

H.M.Jr: Well, I'm glad to call it that.

Eccles: That's part of it. After all, you can't do the job here in the Treasury separate and apart from the rest of the picture; it's just a physical impossibility. And I think unless the thing heads up here under that broad head of fiscal policy and that - the very thing you're talking about is going to upset democracy, that's all. You just cannot have this a hit-and-miss proposition.

H.M.Jr: Well, I'm on record in writing, either two times or three times, that the President should appoint an economic planning committee - either twice or three times - and I haven't got anywhere with it yet. But I did put it in writing.

Eccles: Yes, but after all, an economic planning committee has got to - it seems to me it's got to head up right here.

H.M.Jr: Well, I never suggested that it head up here.

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- Eccles: Couldn't head up anywhere else.
- H.M.Jr: Well, we made a little start today. At least I feel I've had something out of this.
- Hanes: Another job to be done is - which I don't think anybody is attacking concretely - is the matter of coordination of the state and federal tax systems too, because we're taking now about 14 billion dollars out of the economy for taxes - that's what the total of the state and federal tax bill is. Out of a 60 billion dollar income that's one thing; out of 80 billion dollars that's another thing.
- Eccles: That's right.
- H.M.Jr: What we're talking about here - the fact it's never been tried is encouraging - I mean hasn't been tried and failed.
- Ruml: That's right. And we now think we can produce the income that's necessary to take care of our necessities; it's just the income, you know.
- H.M.Jr: Well ...
- Eccles: The danger of a deficit, of course, continuing is the - I get into the monetary aspect of it - simply that it does create an increasing volume of bank deposits. Particularly is that true where you have large excess reserves and there's a constant pressure to invest the reserves and thus create the deposits. Now we have at the present time, of course, a huge volume of deposits, in excess of anything we have had; and with the next twelve months the deficit that's inevitable - we've got this deficit financing, so that we can envision a substantial further increase in deposits through deficit financing without looking into this budget for the next year. Now, private credit expansion has started, it's turned. For a time we had a substantial liquidation. For the last few months it's been right on - pretty level; and it has now started upward. Now, with the increased business activity, the private capital market is opening up and we have refunding and some new issues. The FHA is using a lot of bank credit - private activity. So that there is the indication of a

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substantial possible increase in bank loans and investments outside of Governments, see - I mean outside; so that with the increase in Governments plus the other you get that cumulative effect of a credit expansion, or inflation, you see, within the system. And as the Secretary says, you've got this thing - you're figuring a year and a half ahead, and the one - and with the present volume of deposits you've got, plus a further increase, and with the increase in the volume of credit, you get an increase in velocity - they seem to go together - and we've got here a potential inflationary development that certainly over a year and a half could be a real factor. And in the meantime we've got the stage set so that you're prepared for a huge deficit that has got to be financed. That's the dangerous ....

H.M.Jr: Well, I'd like to go on record here and now: give me a little price inflation.

Eccles: Oh, I think the price inflation ....

H.M.Jr: Give me a little price inflation.

Eccles: The price inflation is fine, if you could get it where you want it. The trouble with the price inflation - where you need it is in the agricultural field, but damn it, where you get it is in the housing field and a few of the bottleneck places; damn it, that's the trouble. We get - what we'll do: railroads will need a lot of equipment next year and following year; they'll want to buy in one year what they held up buying for a period of three years.

Hanes: I wonder, though, if we couldn't compensate those farmers if we had the national income up.

Eccles: That's fine.

Hanes: We could compensate the farmers.

Quail: The estimates are quite striking ....

Eccles: But that takes taxes. Pull the taxes from the higher group and put it into the farmers; that's fine.

Haas: with any move in credit expansion such as you have



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described, agricultural prices, even despite surpluses, would improve considerably. Take cotton, for example.

Eccles: It would help agriculture, particularly the fruit and vegetable and meat and dairy products.....

Haas: Cotton also.

Eccles: ...where there is a very much larger possible domestic consumption. Of course, there could be some expansion in cotton domestically.

I agree that a real expansion in the general business activity will influence to some extent farm products.

Haas: It has every time in our history to date.

Eccles: But if other prices go up faster or even as fast as farm products, they're not benefited much by the increase.

Ruml: What you say raises a point I'd like to ask Mr. Bell about. It would seem to indicate the great desirability, if it's legally and logically possible, of having a considerable amount of flexibility in your program both for income and expenditure. Is that practically impossible to get?

Bell: Well, it's almost impossible on your income side unless you would put a great deal of discretion in the Secretary with respect to rates of taxes, and then you would probably have to apply them to the miscellaneous excise taxes so they could be cut off within 30 days or added within 30 days - something like that. On your expenditure side the regular departments can be controlled to some extent, but not in a large amount of money; maybe to the extent of half a billion dollars a year. But your real flexibility comes in your WPA, CCC camps, and things of that sort. The trouble has always been over the past five years in your WPA program that it's always - expenditures have always been made right at the time when you didn't want them; and that's exactly what's going to happen this time.

Ruml: We've been studying, as you know, the various public works things in the Resources Committee over a period of years, and I was appalled to see the small amount of

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flexibility. I think the optional items only amounted to a billion and a quarter. Well, that's a very small amount to play with in a period of six years. It would seem to me that certainly on a lot of the erosion stuff, and these - this stream stuff, the water-jet stuff - a lot of things could be gotten ready that could be either turned on or off, depending on budgetary exigencies.

Bell: It's pretty difficult to start a project like flood control and ...

Ruml: Oh, flood control ....

Bell: ...river and harbor improvement and then stop it when the upswing comes, because you get your local community interested in it and politics then bring pressure to bear; you just can't stop those things.

Ruml: That's perfectly true, but I've seen some of the things and they're rather small amounts in the individual items; on some of the upper streams, you know - I mean twenty-five, thirty-five thousand dollars, that sort of thing. If you get a whole bunch of those things, you could play the organ, so to speak.

H.M.Jr: Well.. - you (Bell) want to say something?

Bell: Go ahead.

H.M.Jr: Now, you take, for instance, the program we're in now. Every dollar that Congress gave us for Mr. Ickes is allocated, isn't it?

Bell: Practically. I have figures on that if you want to ...

H.M.Jr: Well, we're talking - let's have the figures.

Bell: Out of Mr. Ickes' 950 million dollars, you recall, there was 200 million dollars available for allocation to the Federal departments. Of that 200 million, 196 million dollars has actually been allocated, and the other four million is in the mill. And that's all or practically all under contract and going.

Now, of Mr. Ickes' 750 million dollars available for loans and grants, he has made allotments up to October 17 of 47 million dollars for loans and 633 million

-30-

dollars for grants, making a total of 681 million. He has sent offers to the applicants, out of that 680 million, of 546 million, including both loans and grants. The offers that have been accepted are 427 million. The bids have been advertised for 204 million; contracts have been awarded for 199 million, and there are actually under contract and going 180 million. Now that shows you how fast this public works can get started.

H.M.Jr: Well, to answer your question, the thing which I have learned after four years in this chair: you get your bill through for public works the way we did this time in June; you don't reach your maximum expenditure until a year later.

Bell: That's right.

H.M.Jr: The way things are going now, I'm convinced we didn't need it - the Ickes money - and we could have got what we got without it. Maybe wrong, but I still believe that. I believed it at the time and I still believe it. Not asking for any arguments, though. Anyway, comes along June and we're spending at the rate of 12 billion dollars. Now, if we don't need it and I should be right, it may choke off private industry at that time. It may. But the point that I'm making is that it starts a year after we vote it, and you recognize - let's say that you wanted it six months earlier; so it takes about 18 months until it gets going, and it takes at least another 18 months to stop it. Doesn't it?

Bell: After you once enter into your contracts, just can't cut them.

H.M.Jr: Runs into what, - '40, '41?

Bell: Yes, extends into '41 - public works contracts.

H.M.Jr: So the thing we decide - the only kind of money that Bell and I can start quickly and stop quickly is the kind of money that Hopkins spends. We can turn that off or on within a month. We've seen them do it.

Eccles: If you get enough of that consumer buying power, then you get - build the national income up; then you get the private capital expenditure.

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H.M.Jr: You can turn that off and on almost within a month, can't you, Dan?

Bell: Yes, sir.

Ruml: The trouble about that is, Mr. Eccles, from a human resources point of view it's poor money to spend, because it's demoralizing.

May I ask you this question? It would be helpful, wouldn't it, if you had a larger field to play in than you have as a matter of fact? I mean if the Ickes stuff could be used, if some taxes could be used that way, it would be helpful, wouldn't it? It might be worth while studying some possibilities there.

H.M.Jr: Very. Because we're limited now. We haven't changed a bit. Takes 18 months to get Mr. Ickes started, takes 18 months to stop him. I may be off a couple months, but that's roughly right.

Bell: That's right, yes, sir.

H.M.Jr: What? I mean if you people can develop something else besides Mr. Hopkins' type of work which can start within, say, six months, stop within six months, it would be a great improvement. What?

Ruml: Yes, be a great improvement.

Delano: Well, the housing works a great deal better than that, doesn't it?

H.M.Jr: Slow.

Bell: Slow. They were going to start, Mr. Delano, last spring. Now it's January 1. When you get to January, it will be April 1.

Ruml: The fastest thing in the world would be the gasoline tax.

H.M.Jr: If I'm right, the last figures I saw, Straus had not actually spent three million dollars, had he?

Bell: I think he spent a little more than that, but he - they hadn't even spent the 25 million we gave them as a

-32-

credit line.

H.M.Jr: He's actually spent about what?

Bell: I'd say between five and ten.

H.M.Jr: The last I saw was less than three.

McR: That include his administrative expenses, Dan?

Bell: Yes - first of January, somewhere along there.

H.M.Jr: Oh, that includes his administrative expenses.

Bell: Yes, sir.

Taylor: Wagner Act was passed in August the year before.

Bell: Yes.

H.M.Jr: If we've got a - if we're going to do this thing.... Two things that I see that you've pointed out to be very helpful: one, a new technique which we haven't got - no one's been smart enough - something in between an Ickes type of work and a Hopkins type, something - I mean as to time; and then the other thing, which I'm very much interested in, is on this type of public works which do not appear in the budget. And I know the President's interested in that because he's asked us again and again. Huh?

Delano: Well ...

H.M.Jr: If you (Ruml) could stay behind with Haas, and maybe in about another week or so, when you think you've got something - when do you usually come down? I know you have visiting days.

Ruml: Usually the week-end. Any day except Thursday would be better for me, because of the New York Bank which meets Thursday.

H.M.Jr: Well, how about next Friday, a week from Friday?

Ruml: A week from Friday would be fine.

H.M.Jr: Would that cramp anybody?

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Eccles: A week from tomorrow?

H.M.Jr: Yes.

Ruml: That's better than Monday for you?

H.M.Jr: Monday is a bad day.

Ruml: Is Tuesday so bad?

H.M.Jr: This particular Monday I wouldn't have anything.

Ruml: I was thinking ...

H.M.Jr: .. generally?

Ruml: ... generally Monday is all right.

Bell: Be November 1 and November 2.

H.M.Jr: Would you go over to Monday, October 31?

Ruml: That would be better, yes.

Bell: That's all right.

H.M.Jr: Would you (Eccles) rather do it that way?

Eccles: Any day suits me.

H.M.Jr: We'll say 10:15 Monday, October 31. That suits you (Ruml)?

Ruml: That suits me fine.

McR: A week from next Monday.

Ruml: I have stated meetings next Thursday and Friday.

H.M.Jr: 10:15 October 31.

Bell: 10:15.

H.M.Jr: Is that all right with everybody? But you and George Haas have got to do a little home work between now and then.

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- Ruml: Also some members of our technical committee.
- H.M.Jr: And maybe - may bring in some ....
- Eccles: We've got some people, I think, that we can put to work on various phases of this to possible good advantage.
- Haas: That's right, particularly problem one.
- Ruml: We'll at least make a report of progress.
- H.M.Jr: At least as far as Bell and I are concerned, and I guess Hanes, we won't have anything new then unless the President gives us something new; then if he does, we'll lay it on the table, you see?
- Bell: I wondered if the National Resources Committee had done any work as to how much money could be spent on Government plant? For instance, we own two hundred million acres of ground. What could we do to improve all that?
- Ruml: We have done ....
- Bell: That's the best type of expenditure you could get.
- Ruml: We've done a lot of watershed work.
- Bell: Watershed work, to control the ...
- Ruml: Exactly.
- Bell: I'd much rather see that in the state and local, because they step out from under when we quit; we're maintaining about half of the cities in the country on that now, and it's not additional money spent, it's substitute money.

October 20, 1938

TELEGRAM (OVER WHITE HOUSE WIRE)

COL. MARVIN H. McINTYRE  
NELSON HOUSE  
POUGHKEEPSIE NEW YORK

PLEASE REMIND THE PRESIDENT THAT HE PROMISED TO SEE  
HANS BELL AND MYSELF ON MONDAY AFTER LUNCH IN CONNECTION  
WITH THE BUDGET AND TAXES STOP WOULD APPRECIATE HAVING  
THIS APPOINTMENT

HENRY MORGENTHAU JR



**Treasury Department**

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**TELEGRAPH OFFICE**

15 PO E TWS PAID

PTY NEWYORK NY 430P OCT 20 1938

1938 OCT 20 PM 5 20

HON HENRY MORGENTHAU

WASHN

THE FIRST DRAFT OF THE TREASURY ARTICLE IS FINISHED AND IN ALL PROBABILITY WILL BE MAILED TO WASHINGTON TONIGHT, WOULD YOU MIND ADVISING US AT ONCE COLLECT WHERE WE SHOULD SEND IT, THE REASON WE ASK IS THAT TIME IS RUNNING SHORT AND WE WOULD GREATLY APPRECIATE A PROMPT READING ON YOUR PART.

RUSSELL DAVENPORT FORTUNE

520P

Treasury Department  
Division of Monetary Research

357

Date.....October 20.....1938

Secretary Morgenthau

Mr. Chen gave me the appended list of expenditures, just received by him, which his government will need to make during the next twelve months if they have the foreign exchange available for the purchases. He indicated that they would prefer to make those purchases from the United States, if possible.

I thought you might like to see this at once inasmuch as it might have some bearing on the problem before you.

MR. WHITE  
Branch 2058 - Room 200

October 20, 1938

Following is translation of Cable received from His Excellency Dr.H.H,Kung showing urgent requirements:

(1)	Aircrafts, Equipments, Spare Parts Gasoline, Oils, and Aviation Gas .....	US\$	35,400,000
(2)	Transport Department, Ministry of War:. Various kinds of Gasoline & Oils .....		9,509,000
(3)	Ministry of Communications: 3000 3-ton Trucks, 1000 6-ton Trawleys, and Spare Parts .....		8,250,000
	Transport Department: 4880 Light Trucks, 880 Heavy Trucks, 50 Heavy Engineering Units 100 Light Engineering Units <u>500 2-Wheel Units</u> .....		6,600,000
	10 3 F Mechanical Units 40 3 F Light Repair Units <u>10 2 ? F Supply Units</u>		180,000
	200 Oil Tank Truck Chassis, etc.		400,000
(4)	Armaments and Ammunitions .....		85,400,000
	Telegram & Wireless Apparatus .....		3,500,000
	Total	(Approx.)	<u><u>US\$ 149,239,000</u></u>

Detailed particulars sent by Airmail on October 17th.

Kunming, Yunnan,

20th October, 1938

The Honorable

Secretary Henry Morgenthau, Jr.,

Department of Treasury,

Washington, D.C.

Dear Mr. Secretary,

I enclose reports typed from notes sent me by Dr. Buck  
from Chungking.

Respectfully,

*Enid Saunders*Enid Saunders  
Secretary to Dr. Buck

RECEIVED  
NOV 2 1938  
OFFICE OF THE SECRETARY  
KUNMING, YUNNAN, CHINA

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RECEIVED  
NOV 2 1953  
OFFICE OF THE SECRETARY  
AMERICAN DEPARTMENT

October 7th and 13th, 1938

To Secretary Morgenthau

From J. Lossing Buck

INTERVIEW WITH MINISTER KUNG

Minister Kung was in bed with malaria the first time I saw him, and the second time he had caught cold.

He spoke favorably of your negotiations with K. P. Chen in Washington.

In regard to the Canton attack he states: "The young officers who have not yet had a chance want an opportunity to loot South China. The Japanese are very fond of all Chinese art."

In reply to my question whether or not there was any hope of assistance from England, he said: "England is only willing to send us some of her commodities. I am disgusted with the way England has acted. I am not interested in buying her commodities. She ... well, I don't like to use such harsh language.

"We have a number of Russian advisers taking the place of the German advisers; also many technicians to help us use their equipment. There are about 300 Russians in the aviation corps. The Russians are not as good as the Germans."

Speaking of independence movements of the provinces in the past, Minister Kung compared his policy with that of T. V. Soong. He said: "Soong kept all his finances secret, and refused help to the provinces. This caused

suspicion on the part of the provinces which were refused financial aid, and led such provinces to believe that the Central Government was trying to minimize their influence. My policy has been to help finance the provinces, make the condition of the central finances known, and in this way bring the provinces within the fold of the Central Government.

"I have organized a Southwest Economic Development Commission, with the hope of improving the economic situation in that part of the country. We have just had a Transportation Conference to improve transportation facilities. The shorter road from Yunnanfu to Szechuen (above the River from Chungking) will be completed by the end of the year."

October 15th, 1938

To Secretary Morgenthau

From J. Lossing Buck

CHINESE FOREIGN EXCHANGE

Dr. Arthur Young of the Central Bank states that: "The flight of capital has greatly decreased, and it is much easier to hold the exchange rate. The balance of trade has been brought into very satisfactory relationship through trade control."



October 8th, 1938

To Secretary Morgenthau

From J. Lossing Buck

RUSSIAN TRADE AGREEMENT WITH CHINA

T. S. Miao, head of the Foreign Trade Commission at Chungking, states that he is in difficulty with the Russian Embassy officials here in Chungking over the 50 million yuan barter agreement with Russia. Russia agreed to supply armaments and China agreed to deliver products, chiefly tea, to the extent of 20 million yuan, and the remainder in cash. The agreement is for three years. Mr. Miao states China finds it impossible to deliver tea at the specified time because of the difficulty of obtaining coal, labor (due to conscription), and even tea, at the points where the tea must be processed into tea bricks. The Russian officials are pressing the Chinese because of non-fulfilment of their part of the contract, whereas the Russians have already delivered large quantities of armaments.

October 10th, 1938

To Secretary Morgenthau

From J. Lossing Buck

PRICES IN CHINA

Wholesale prices in Shanghai have advanced from 126 for July, 1937, to 153 for July, 1938, when 1926 = 100.

In Canton wholesale prices have advanced from 116 for July, 1937, to 147 for July, 1938, when 1926 = 100.

In Chungking (Szechuen) wholesale prices have advanced from 95 for July, 1937, to 131 for July, 1938, when 1937 = 100. On September 5th, 1938, they had further advanced to 137. Food has dropped from 95 for July, 1937, to 86 for September 5th, 1938. Clothing has increased from 97 for July, 1937, to 185 for September 5th, 1938.

Wholesale prices in Chungking (1) of Szechuen products, advanced slightly from 94.9 in August, 1937, to 100.1 on August 5th, 1938; (2) of commodities imported from other provinces advanced from 103.2 for August, 1937, to 205 for August 5th, 1938; (3) of articles imported from abroad advanced from 108.2 for August, 1937, to 240.9 for August 5th, 1938.

Wholesale prices in Chungking, according to stage of manufacture, have indices on August 5th, 1938, as follows: raw materials 80.5; semi-manufactured materials, 137.4; and manufactured goods, 188.5.

Cost of living in Shanghai has risen from 120 for July, 1937, to 151 for July, 1938. Cost of living in Chengtu has decreased slightly, from 93.3 for August, 1937, to 91.5 for August, 1938.

October 13th, 1938

To Secretary Morgenthau

From J. Lossing Buck

#### CANTON ATTACK

The apparent impending attack on Canton is worrying T. S. Miao of the Foreign Trade Commission, as the Commission has three to four million yuan in export products along the Canton-Hankow Railway. He is very much upset as to how to save these products, and has worried over his plans these last few days as to how to rush products to New York in response to negotiations with K. P. Chen.

Mr. Li, who has supervision of transportation, is worrying about containers for wood oil. Kerosene tins have advanced to over a dollar per tin. Local people have lost the art of making barrels of the type that was first used in the wood oil trade.

Transportation for both imports and exports will be greatly limited with the closure of the Canton-Hankow Railway to Hong Kong, and the closure of the Pearl River.

October 15th, 1938

To Secretary Morgenthau

From J. Lossing Buck

ASSISTANCE OF FOREIGN POWERS TO CHINA

Dr. Chen Chia-tsun, in charge of foreign exchange control for the Foreign Trade Commission, is interested in international politics as related to China. He feels that China cannot win the war without substantial aid from abroad. He is afraid England may bring pressure to bear on China to force a settlement unfavorable to China, and in that case he queries: "Will America support England?". He also states that there is a school of thought that China long ago should have thrown in her lot with Russia. There is already a feeling among most Chinese that Russia has given more substantial help than any other country.

October 11th, 1938

To Secretary Morgenthau

From J. Lossing Buck

LUNCHEON WITH AMBASSADOR JOHNSON IN CHUNGKING

The office of the American Embassy is located in a very ordinary building on the edge of the Yangtze opposite Chungking. The Ambassador lives in an Asiatic Petroleum residence on a hilltop about ten minutes by sedan chair from the office. He himself admits that when he gets on this hill he does not like to leave it. Mr. Peck, his Councilor, remarked that the Ambassador may be physically somewhat indolent, but we can all agree that he is mentally alert.

The Ambassador asked me whom I saw in Washington. Among others I spoke of seeing the head of the Far Eastern Division of the Department of Commerce. The Ambassador asked: "What does he think about things out here?" I said: "He is interested, and ..." . Before I could finish the Ambassador said: "Being interested reminds me of a dog I used to have, which was very interested in rats. He would watch for them actively, but would never do anything about catching them. That is the way they are back in Washington, isn't it, Mr. Peck?" (Mr. Peck was in Washington in the spring and late summer of this year.) Mr. Peck replied: "Yes, that describes the attitude very well." (Presumably Mr. Peck's contacts were mostly in the State Department. This is the first indication I have had from the Ambassador indicating his interest in a more active policy, and for this reason I pass it on to you.)

Mr. Peck remarked: "What I want to know is what K. P. Chen is doing in Washington. Has the silver agreement been renewed?" I replied that I understood that it had been, but beyond that it was unnecessary for me to say more.

October 10th, 1938

To Secretary Morgenthau

From J. Lossing Buck

## INDEPENDENCE MOVEMENTS IN CHINA

Mr. Eigener, the Trans-Ocean News Service representative in China, states that there is a great deal of talk among foreigners and some Chinese about a declaration of independence by Szechuen province, and an attempt by the Communists to gain control of the government, if Hankow falls.

I gather that this opinion in regard to Szechuen is more supposition than anything based on a real inside knowledge. Undoubtedly some military officials in Szechuen would like independence, but wanting it and being able to obtain it are two very different things. Public opinion would be so strongly against it, and in support of the Generalissimo that an independence movement, even if attempted, would be of short duration. Y. L. Tsu, of the Kweichow government, states that there is no danger of an independence movement in Szechuen.

Ambassador Johnson states that foreigners must have something to gossip about at their clubs and around their bars. They pose as political experts, whereas they really know little of which they speak. The Ambassador does not consider that there is any real danger of an independence movement, although he does feel that the present unity is one from outside pressure, and therefore might not be permanent.

OVEN  
 HENRIARD VS  
 RECEIVED IN CORRESPONDENCE DIVISION



## TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE October 20, 1938

TO Secretary Morgenthau  
FROM Mr. Haas *EA*  
Subject: The Government's Fiscal Problem

Summary and Conclusions

1. The excess of the present level of expenditures over the average of the years 1928-1932 is due primarily to new classes of outlays, which were altogether missing from the pre-1933 budgets.

2. The maintenance of a level of Federal expenditures approximating \$8.4 billions, exclusive of scheduled increases in self-supporting old-age pension outlays, but inclusive of \$600 millions for debt retirement, appears likely, even after considerable business recovery has been achieved.

3. The present tax structure will not balance the anticipated budgetary requirements of a future "normal" year, except at levels of the national income substantially above any yet achieved.

4. Although the previous deficits and increases in debt have not strained the Government's credit, and although the practical limit to the size of the public debt is extremely flexible, the credit position of the Government is likely to become increasingly vulnerable, unless the tax structure is substantially strengthened.

5. A complete early balancing of the budget by drastic tax increases is unnecessary and would be unwise. A tax bill that raised \$500 millions to \$800 millions of additional revenues would constitute ample immediate progress in this direction.

6. In the long run, the new social responsibilities that have been assumed by the Federal Government during recent years will be supported by tax revenues or they will be abandoned.

Secretary Morgenthau - 2

I. The Expenditures Side of the Picture

1. Present level of expenditures due primarily to new functions:

An effective approach to the Government's fiscal problem is to compare the average annual expenditures, by classes, of the five years 1928-1932, inclusive, with the revised budget estimates for the current fiscal year (1939). This is done in Table I and Chart I.

It is striking to note that, of the total net expenditures, excluding debt retirement, of \$8,985 millions budgeted for the current fiscal year, the following items, which were altogether missing from the pre-1933 budgets, account for nearly one-half:

	(Millions of dollars)
Direct relief and work relief	2,284
Civilian Conservation Corps	275
Agricultural adjustment program	700
Social Security and Railroad Retirement	833
Public Works Administration grants and administrative expenses	<u>355</u>
Total	4,447

In other words, about four-fifths of the amount by which the anticipated net expenditures for 1939 will exceed the average for the years 1928-1932, inclusive, is attributable to the new classes of outlays listed above.

2. Drastic cuts unlikely in older classes of expenditures:

Although the older classes of expenditures will in the aggregate be approximately \$1,000 millions greater in 1939 than the average of the years 1928-1932, inclusive, the possibilities of drastic reductions therein appear to be limited. The outlays for national defense and for interest on the public debt, for example, both seem headed for significant increases in the near-term future. This will be

Secretary Morgenthau - 3

true of the cost of the public debt -- unless substantial budgetary surpluses soon appear -- even if interest rates generally continue at their present levels, because of the 3 percent rate that must be paid on obligations issued to the Old-Age Reserve Account. Further, it would be surprising, in view of our traditions, if our outlays for veterans' pensions do not increase substantially. The chief opportunities for savings in the older classes of expenditures appear to lie in the field of public works, where the 1939 outlays, exclusive of the Public Works Administration, are scheduled to aggregate some \$676 millions, as compared with an average of \$308 millions in the five years 1928-1932, inclusive.

3. Substantial cuts possible in certain newer classes of expenditures, though others are likely to increase:

(a) The Civilian Conservation Corps appears to be here to stay, at an annual cost of about \$300 millions.

(b) The agricultural adjustment program, scheduled to cost \$700 millions during the present fiscal year, seems likely at the moment to continue to absorb some such sum in one form or another for some years to come.

(c) The Public Works Administration grants might be eliminated, with a saving of \$355 millions in grants and administrative expenses.

(d) Direct relief and work relief may conceivably be abandoned altogether at some future date, with a budgetary saving on the 1939 basis of \$2,284 millions. From an immediate budgetary standpoint, such abandonment would constitute the greatest step toward a balanced budget that could be taken at this time. A major issue of public policy, however, is involved in this question; hence, it cannot be disposed of on the basis of budgetary considerations alone. The President has propounded the doctrine that States and cities must take care of their unemployables, but has conceded the responsibility of the Federal Government for aid to victims of involuntary unemployment. If this policy is continued, sharp reductions may nevertheless be made in the outlays for relief in times of good business; but relatively large sums would still be required of the Federal Government. A reduction to the level of one billion dollars annually would be a considerable achievement.

Secretary Morgenthau - 4

(e) Social security expenditures are rising rapidly and will continue to do so for some years to come. The largest part of these outlays -- for the Old-Age Reserve Account and Railroad Retirement -- is at present considered to be self-supporting because it is supposed to be balanced by current and scheduled increases in special taxes already on the statute books.

There is reason to believe, however, that the scheduled rate increases in these special taxes will not be sufficient to meet the full actuarial costs on a reserve basis if advantage is taken of some technical weaknesses of the Social Security Act. Despite this fact, there is a growing body of opinion that seeks a liberalization of the benefit provisions of the Act without commensurate, if any, increases in the special social security taxes. This problem is sufficient in size and in complexity to merit independent and extended treatment (which is now in process). It will be assumed here for our present purposes, that existing provisions for rising payroll taxes will be sufficient to meet the increasing outlays that will be required for the contributory systems.

It is not widely recognized that, in addition to the so-called self-sustaining Federal expenditures under the Social Security Act, the Federal Government is committed to growing outlays for grants to the States for old-age assistance, child welfare, and the like; and that, unlike the scheduled increases in other social security expenditures, these grants are not covered by any special statutory provisions for increased revenues. These uncovered social security expenditures, which amounted to about \$230 millions in the fiscal year 1938, and are estimated at \$277 millions for the fiscal year 1939, are tentatively expected to rise above \$550 millions by 1945.\*

It seems clear, therefore, that increases, rather than decreases, are to be expected in the field of social security expenditures.

4. Maintenance of high level of total Federal expenditures seems probable:

It is an historical fact that new high levels of Federal expenditures, once achieved, tend in large measure to be maintained. The following totals of Federal expenditures

---

\* For the fiscal year 1938, however, receipts from the special taxes levied under the so-called self-supporting provisions were in excess of the expenditures thereunder, including transfers to the Old-Age Reserve Account and the Railroad Retirement Account; and for this reason, the net total budgetary outlay for social security in excess of payroll tax receipts was only \$80 millions, exclusive of refunds. For the same reason, the net total budgetary outlay for the fiscal year 1939 is estimated at \$241 millions, instead of \$277 millions.

Secretary Morgenthau - 5

for recent years, exclusive of outlays for the prepayment of the bonus and for debt reduction, constitute a striking series:

	(Millions of dollars)
1928-1932 average	3,538
1933	3,864
1934	6,011
1935	7,010
1936	6,992
1937	7,886
1938	7,626
1939 (Budget Summation estimate)	8,985

In accordance with the preceding analysis, let us assume that we can look forward in the next few years to the following reductions from the estimated 1939 level of expenditures:

	(Millions of dollars)
Public Works Administration grants and administrative expenses entirely eliminated, saving	355
Total public works expenditures reduced to \$500 millions, resulting in a saving of	176
Direct relief and work relief expenditures reduced to a level of \$1,000 millions, thereby saving	<u>1,284</u>
Total cuts	1,815

Partly offsetting these cuts are certain increases that should be allowed for (apart from increases in the self-supporting elements of the social security program, which may be ignored for the present purpose):

	(Millions of dollars)
Social security grants to States	300
National defense	200
Interest on the public debt	100
Civilian Conservation Corps	<u>25</u>
Total increases	625
Total net reduction	<u>1,190</u>

Secretary Morgenthau - 6

If this total net reduction of \$1,190 millions be applied to the estimated expenditures for 1939, we arrive at an expenditure level, exclusive of Sinking Fund outlays, of \$7,795 millions, to which we should add approximately \$600 millions for the annual Sinking Fund requirement, thereby arriving at a grand total of \$8,395 millions.

In other words, a balanced budget with full statutory provisions for the Sinking Fund may be expected to require total annual receipts approximating \$8,400 millions -- leaving out of consideration the future increases in receipts and expenditures arising out of the old-age provisions of the Social Security and Railroad Retirement Acts.

Table II compares the classified expenditure estimates for 1939 with those that would be the case in a subsequent "normal" year if the increases and decreases cited in the foregoing were to be effected, with scheduled self-balancing increases in the receipts and expenditures under the old-age provisions of the Social Security and Railroad Retirement Acts ignored.

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## II. The Revenue Side of the Picture

### 1. Tax structure greatly strengthened in recent years:

Back in the years 1926-1930, inclusive, the national income paid out averaged \$74.4 billions, and total Federal receipts averaged \$4.1 billions. Today, if the national income were to reach the same level, total Federal receipts could be expected, on the basis of extremely rough and tentative estimates prepared in this Division, to be about \$6.1 billions, exclusive of payroll taxes, or about 50 percent more than the average of 1926-1930, inclusive. This is a rough measure of the extent to which Congress has strengthened the productiveness of the tax structure in recent years.

### 2. Present tax structure will not balance the budget except at new high levels of national income:

The strengthening of the tax structure has not kept pace with the growth of Federal expenditures. The latter, on the basis of the reduced level of our "normal" year, and exclusive of self-supporting social security expenditures and debt retirement, would exceed the average annual expenditures of 1926-1930, inclusive, by some 136 percent.

The rough tentative estimates prepared in this Division indicate that the existing tax structure, exclusive of increases in payroll taxes, will not yield \$8,400 millions of revenues except at levels of the national income never yet achieved in the Nation's history. This is indicated in Chart II. It will be noted that, whereas the national income paid out in the peak year 1929 was \$78.6 billions, a national income of about \$87 billions would be necessary to produce \$8,400 millions of revenues from the present tax structure (exclusive of increases in payroll taxes) -- assuming the correctness of these tentative revenue estimates.

### 3. Estimates of increased tax revenues required to balance the budget at various levels of national income:

If we assume that the average national income during the next ten years will slightly exceed the average of five of the highest years in our previous history (1926-1930, inclusive), we arrive at a figure of about \$75 billions. A

Secretary Morgenthau - 8

national income that averaged this level over a 10-year period could conceivably go as high as \$100 billions in one or more years, as well as substantially below the average in other years. During the ten years ended in 1937, the average national income amounted to \$62.2 billions. A working estimate of \$75 billions as the average national income during the next ten years would not, therefore, be unduly pessimistic.

As is indicated in Chart II and Table III, a \$75 billion national income could be expected to produce annual tax revenues, from the existing tax structure, of \$6.8 billions, exclusive of increases in payroll taxes. Such a yield would fall short by \$1.6 billions of the \$8,400 millions roughly estimated in the foregoing to be required to balance the budget, with full provision for statutory Sinking Fund expenditures, but exclusive of scheduled increases in self-supporting old-age benefit outlays, in a "normal" year. If the national income averaged \$80 billions, the annual shortage in tax receipts would approximate \$1 billion; and at \$85 billions, there would still be a shortage of \$300 millions after allowing for full statutory Sinking Fund expenditures.



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### III. The Deficit and Debt Side of the Picture

#### 1. Tenth successive annual Federal deficit in prospect:

The Presidential budget message to be delivered to Congress next January will forecast the tenth successive annual Federal deficit. The cumulated deficit, exclusive of debt retirement, of the past eight completed fiscal years approximated \$20 billions. The deficit for the current fiscal year is estimated at slightly less than \$4 billions, exclusive of debt retirement. The prospective deficit for the next fiscal year likewise approximates \$4 billions, exclusive of debt retirement.

The gross public debt has increased by almost \$21 billions during the past eight completed fiscal years, and is likely to be increased during the current and next fiscal years by approximately the amount of the deficits for those years, or by about \$5 billions.

#### 2. Previous deficits and debt increase have not strained Government credit:

Despite the magnitude of the deficits and of the Federal debt increase during the past eight years, there is no evidence that the credit of the Government has been strained or that the net economic effects have been other than beneficial. Bank purchases of Government obligations served to replace a large volume of bank deposits that had been destroyed through the previous deflation.

Inflationary consequences did not ensue, partly because confidence was maintained in the Government's financial capacity and integrity, and partly because the volume of deficit spending was well within the country's capacity to produce at the existing price levels. The consideration that a very important fraction of the deficit expenditures went for useful public works was not lost upon investors.

Finally, despite political criticism to the contrary, the Administration obtained widespread adherence to its view that the deficits were temporary, and that the debt increase would be erased through subsequent budgetary surpluses. The repeated and partially successful efforts of the President to strengthen the tax structure have been important in adding to public confidence in the financial integrity of the Government.

Secretary Morgenthau - 10

The fact that the Government has been able to borrow at very low rates of interest is to be explained not only in terms of public confidence, but also in terms of the monetary and banking measures and developments which created unparalleled ease in the banking structure, and in terms of the relative absence of competing demands for credit from private industry.

3. Practical limit to size of public debt extremely flexible:

The practical limits to the expansion of the public debt are not the same under all circumstances and cannot readily be estimated in advance. Great Britain, with a population approximately one-third that of the United States, and with a national income less than one-third as large, has accumulated a public debt of about \$40 billions. A mechanical inference, therefore, might be that the United States can stand a public debt of at least \$120 billions. It is highly probable that we could, if this total debt were incurred over a period of 200 years, as has been the case with Great Britain. An increase to any such level in a relatively short space of time, however, might prove to be impractical, save under the spur and coercion of war. The practical limit to increases in the public debt will also vary with monetary and banking conditions, the demands for private capital, the confidence of investors in the party in power, etc.

Of far more immediate importance than the possible absolute limit to the size of the public debt is the rate of increase in such debt and the purposes for which the increases take place. Very large and rapid increases are practicable in wartime, both because of the coercion that is employed in the sale of Government securities and because of the expectation that the end of the war will usher in a period of debt reduction. In times of peace, a low level of private business may permit large and rapid expansion of the public debt for useful public works, and even for direct relief. A continued rapid rate of increase in the public debt during periods of business recovery and prosperity, however, is capable of creating alarm and therefore disruption in the investment markets, because it is interpreted as evidence of the unwillingness or inability of the Government to put its house in order.

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4. Is our deficit and debt position becoming vulnerable?

Unless steps are soon taken to increase the productivity of our revenue structure, there is reason to believe that our deficit and debt position will become increasingly vulnerable to loss of public confidence. This is entirely possible even though our total public debt does not rise above absolute levels well within the means of the country, and relatively lower than those of other countries.

The danger arises from the fact that, without additional taxes, even a substantial increase in the level of the national income will leave the Government's budget sharply out of balance; and from the further fact that the budget for 1940, which will be presented next January, is likely to forecast as large a deficit as any that we have experienced since the onset of the depression. Many will interpret this as indicating that no net progress whatever has been made to date toward the achievement of a balanced budget.

The unsettled international conditions now obtaining, which are recognized to be fraught with the danger of war, will accentuate the vulnerability of the Government's credit position unless progress toward a balanced budget is soon made, because of the actual and potential additional demands upon the Government -- for new armaments at the minimum, and for active war at the maximum -- that these conditions create.

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#### IV. Considerations of Public Policy

##### 1. Complete balancing of budget in near-term future unnecessary:

To maintain unimpaired confidence in the Government's financial position, a complete balancing of the budget in the near-term future is by no means essential. It is only necessary that substantial progress in this direction be recorded. This progress, if the estimates made herein are not too grossly inaccurate, is unlikely to be achieved by reliance upon either reduced expenditures or business revival, or even both: A substantial strengthening of the tax structure appears to be inescapable.

It would be unwise and inexpedient, in our opinion, however, to attempt to impose sufficient new taxes at one time to close the entire gap between the anticipated income and out-go. A tax bill that attempted to do this at one fell swoop would probably be too shocking to the country and might easily involve hasty, arbitrary, and unfortunate decisions with respect to particular taxes. Moreover, it cannot be emphasized too strongly that the revenue estimates made herein are extremely rough and tentative and may err very considerably on the side of conservatism.

In the light of these considerations, it would seem wise to limit the immediate goal to some \$500 millions to \$800 millions of additional tax revenues; and to press for further increases in taxes at a future date when the needs can be more carefully assayed and when some small backlog of experience will have been accumulated on the effects of the first instalment of tax increases.

##### 2. Permanent financial support needed for social responsibilities assumed by Federal Government in recent years:

The continuance of the social responsibilities that have been assumed by the Federal Government during recent years, not to speak of their expansion, depends upon adequate provision for their regular financial support. Thus far, they may be said to have been financed largely by borrowing. In the long run, they will be supported by tax revenues or they will be abandoned.

Attachments

Table I

## Classified Expenditures (Revised Budget Basis\*)

Average of fiscal years 1928-32, inclusive,  
compared with Budget Summation estimates for 1939

(In millions of dollars)

	: 1928-32 : : average :	: 1939 : : Budget : : Summation : : estimates :	: Increase
<b>Regular operating expenditures:</b>			
Legislative, judicial, and civil establishments .....	832	1,113	281
National defense .....	666	1,022	356
Veterans' pensions and benefits ..	829	539	- 290
Interest on the public debt .....	656	976	320
<b>Total .....</b>	<b>2,983</b>	<b>3,650</b>	<b>667</b>
<b>Public works (excluding PWA):</b>			
Public buildings .....	47	65	18
Public highways .....	132	235	103
Rivers and harbors .....	82	175	93
Other .....	47	201	154
<b>Total .....</b>	<b>308</b>	<b>676</b>	<b>368</b>
Loans and investments .....	247	212	- 35
PWA (excluding loans) .....	-	355	355
Direct relief and work relief .....	-	2,284	2,284
Civilian Conservation Corps .....	-	275	275
Agricultural adjustment program ...	-	700	700
Social Security and Railroad Retirement .....	-	833	833
<b>Total expenditures (excluding debt retirement) .....</b>	<b>3,538</b>	<b>8,985</b>	<b>5,447</b>
Debt retirement .....	499	100	- 399
<b>Total expenditures .....</b>	<b>4,037</b>	<b>9,085</b>	<b>5,048</b>

Treasury Department, Division of Research and Statistics. October 19, 1938.

\* Revised Budget Basis excludes the expenditures resulting from the operation of the Reconstruction Finance Corporation, the Commodity Credit Corporation, and the Export-Import Bank.

Table II

## Classified Expenditures (Revised Budget Basis\*)

1939 Budget Summation estimates  
compared with estimates for future "normal" year

(In millions of dollars)

	: 1939 : Budget : Summation : estimates	: Future : "normal" : year : estimates	: Increase
Regular operating expenditures:			
Legislative, judicial, and civil establishments .....	1,113	1,113	-
National defense .....	1,022	1,222	+ 200
Veterans' pensions and benefits ..	539	539	-
Interest on the public debt .....	976	1,076	+ 100
<b>Total .....</b>	<b>3,650</b>	<b>3,950</b>	<b>+ 300</b>
Public works (excluding FWA):			
Public buildings .....	65		
Public highways .....	235		
Rivers and harbors .....	175	500	- 176
Other .....	201		
<b>Total .....</b>	<b>676</b>	<b>500</b>	<b>- 176</b>
Loans and investments .....	212	212	-
PWA (excluding loans) .....	355	-	- 355
Direct relief and work relief .....	2,284	1,000	-1,284
Civilian Conservation Corps .....	275	300	+ 25
Agricultural adjustment program ...	700	700	-
Social Security and Railroad Retirement .....	833	1,133	+ 300
<b>Total expenditures (excluding debt retirement) .....</b>	<b>8,985</b>	<b>7,795</b>	<b>-1,190</b>
Debt retirement .....	100	600	+ 500
<b>Total expenditures .....</b>	<b>9,085</b>	<b>8,395</b>	<b>- 690</b>

Treasury Department, Division of Research and Statistics, October 19, 1938.

\* Revised Budget basis excludes the expenditures resulting from the operation of the Reconstruction Finance Corporation, the Commodity Credit Corporation, and the Export-Import Bank.

Table III

Comparison of Estimated Expenditures in Future  
 "Normal" Year with Estimated Receipts at  
 Various Levels of National Income

(In billions of dollars)

Level of national income paid out	Estimated receipts at various levels of national income	Estimated expenditures in future "normal" year	Excess of receipts (+) or expenditures (-)
60	4.9	8.4	- 3.5
70	6.2	8.4	- 2.2
75	6.8	8.4	- 1.6
80	7.4	8.4	- 1.0
85	8.1	8.4	- .3
87	8.4	8.4	-
90	8.8	8.4	+ .4
100	10.4	8.4	+ 2.0

Treasury Department, Division of Research and Statistics.  
 October 19, 1938.

Note: Future "normal" year assumes 1939 level for old-age and  
 railroad retirement tax receipts and appropriations.

## National Income Estimates\*

(In billions of dollars)

Year	:	Amount
1919	:	60.2
1920	:	72.7
1921	:	58.5
1922	:	59.9
1923	:	69.9
1924	:	70.6
1925	:	75.0
1926	:	72.6
1927	:	72.5
1928	:	75.1
1929	:	78.6
1930	:	73.3
1931	:	62.0
1932	:	49.0
1933	:	45.3
1934	:	51.5
1935	:	55.1
1936	:	62.6
1937	:	69.3

\*1919-25 figures are estimates of income produced; thereafter, income paid out.

Source: 1919-25, Simon Kuznets, "National Income and Capital Formation, 1919-1935", National Bureau of Economic Research, 1937; 1926-28, National Bureau of Economic Research, with adjustments; 1929-37, Department of Commerce.



## Federal Receipts by Sources, Fiscal Years 1926-1939

(In millions of dollars)

	1926	1927	1928	1929	1930	1931	1932	1933	1934	1935	1936	1937	1938	1939 Budget summa- tion estimates
Individual income tax .....	879	912	883	1,095	1,147	834	427	353	420	527	674	1,092	1,286	955
Corporate tax levies .....	1,192	1,317	1,301	1,242	1,263	1,026	630	394	480	671	848	1,220	1,476	1,141
Social Security and Railroad Retirement taxes ...	-	-	-	-	-	-	-	-	-	-	-	265	743	592
Estate and gift taxes .....	119	101	60	62	65	48	47	34	113	212	379	306	417	316
Customs .....	579	605	569	602	587	378	328	251	313	343	387	486	359	278
Tobacco and liquor taxes .....	398	397	411	447	461	455	408	446	684	870	1,006	1,146	1,136	1,019
Miscellaneous taxes .....	248	139	136	93	104	65	46	393	604	493	541	624	570	455
Agricultural Adjustment taxes .....	-	-	-	-	-	-	-	-	371	526	72	-	30	45
Non-tax receipts .....	546	654	674	493	552	382	117	225	162	179	216	210	209	199
<b>Total .....</b>	<b>3,961</b>	<b>4,125</b>	<b>4,038</b>	<b>4,034</b>	<b>4,179</b>	<b>3,188</b>	<b>2,003</b>	<b>2,096</b>	<b>3,147</b>	<b>3,821</b>	<b>4,123</b>	<b>5,349</b>	<b>6,226</b>	<b>5,000</b>

Treasury Department, Division of Research and Statistics

October 19, 1938

\*Customs and non-tax receipts on Daily Statement basis; all others on collection basis.

Expenditures by Classes, Fiscal Years 1926-1939 and Future 'Normal' Year  
(Revised Budget Basis\*)

(In millions of dollars)

	1926	1927	1928	1929	1930	1931	1932	1933	1934	1935	1936	1937	1938	1939 Budget estimate	Future 'normal' Year estimate
<b>Regular operating expenditures:</b>															
Legislative, judicial and civil establishments . . .	666.9	589.4	708.6	851.1	798.4	806.9	924.7	713.0	552.2	527.3	774.7	865.4	998.0	1,113.0	1,113.0
National defense . . . . .	579.7	544.4	624.6	678.1	598.2	607.3	684.5	633.6	499.9	656.5	970.5	888.6	968.0	1,022.0	1,022.0
Veterans' pensions and benefits (excluding bonus prepayment) . . . . .	850.5	721.2	723.5	733.1	771.6	942.6	978.8	646.9	554.1	605.9	675.1	571.5	575.0	599.0	559.0
Interest on the public debt . . . . .	831.9	787.0	731.8	678.3	659.3	611.6	599.3	689.4	756.6	800.9	749.4	866.4	755.0	678.0	1,076.0
<b>Total . . . . .</b>	<b>2,729.0</b>	<b>2,687.0</b>	<b>2,788.5</b>	<b>2,940.6</b>	<b>2,927.5</b>	<b>3,026.4</b>	<b>3,221.1</b>	<b>2,664.9</b>	<b>2,362.6</b>	<b>2,680.6</b>	<b>3,073.7</b>	<b>3,191.9</b>	<b>3,467.0</b>	<b>3,650.0</b>	<b>3,950.0</b>
<b>Public works (excluding PWA):</b>															
Public buildings . . . . .	2.1	7.8	5.7	30.5	42.4	67.6	66.2	105.7	78.7	58.1	71.9	75.3	77.0	65.0	
Public highways . . . . .	48.8	92.5	31.1	95.6	89.6	173.8	209.3	178.2	267.9	317.4	263.3	350.6	277.0	235.0	
Rivers and harbors . . . . .	70.3	65.4	72.9	81.4	78.2	89.2	84.6	90.2	124.5	171.6	190.1	197.0	161.0	175.0	500.0
Other . . . . .	3.8	8.2	9.5	10.6	46.8	73.5	38.0	84.6	121.2	166.7	172.7	184.9	205.0	201.8	
<b>Total . . . . .</b>	<b>174.6</b>	<b>173.9</b>	<b>189.2</b>	<b>220.0</b>	<b>258.5</b>	<b>404.1</b>	<b>478.7</b>	<b>458.7</b>	<b>594.3</b>	<b>713.8</b>	<b>678.5</b>	<b>806.5</b>	<b>880.0</b>	<b>676.0</b>	<b>500.0</b>
<b>Loans and investments:</b>															
PWA (excluding loans) . . . . .	-	1.0	-	10.5	157.9	158.4	825.1	190.9	891.1	443.5	94.0	194.9	141.0	212.0	212.0
Direct relief and work relief . . . . .	-	-	-	-	-	-	-	-	18.8	48.9	233.9	272.9	190.0	255.0	-
Civilian Conservation Corps . . . . .	-	-	-	-	-	-	-	370.2	1,520.0	1,924.6	1,254.8	2,067.7	1,627.0	2,254.0	1,000.0
Agricultural adjustment program . . . . .	-	-	-	-	-	-	-	8.8	331.9	479.5	486.3	386.6	326.0	275.0	300.0
Social Security and Railroad Retirement . . . . .	-	-	-	-	-	-	-	-	290.2	743.0	541.6	415.8	372.0	700.0	700.0
<b>Total . . . . .</b>	<b>-</b>	<b>1.0</b>	<b>-</b>	<b>10.5</b>	<b>157.9</b>	<b>158.4</b>	<b>825.1</b>	<b>190.9</b>	<b>891.1</b>	<b>443.5</b>	<b>94.0</b>	<b>194.9</b>	<b>141.0</b>	<b>212.0</b>	<b>212.0</b>
<b>Total expenditures (excluding bonus prepayment and debt retirement) . . . . .</b>	<b>2,903.6</b>	<b>2,857.5</b>	<b>2,969.1</b>	<b>3,171.2</b>	<b>3,141.9</b>	<b>3,670.9</b>	<b>4,515.1</b>	<b>3,863.5</b>	<b>5,011.1</b>	<b>7,009.9</b>	<b>5,992.1</b>	<b>7,865.7</b>	<b>7,626.0</b>	<b>8,985.0</b>	<b>7,795.0</b>
Debt retirement . . . . .	487.4	519.6	540.3	549.6	553.9	440.1	412.6	461.6	399.8	573.5	405.3	104.0	65.0	100.8	600.0
Bonus prepayment . . . . .	-	-	-	-	-	-	-	-	-	-	1,673.5	556.7	-	-	-
<b>Total expenditures . . . . .</b>	<b>3,391.0</b>	<b>3,377.1</b>	<b>3,509.4</b>	<b>3,720.8</b>	<b>3,695.8</b>	<b>4,111.0</b>	<b>4,927.7</b>	<b>4,325.1</b>	<b>5,370.9</b>	<b>7,583.4</b>	<b>9,068.9</b>	<b>8,546.4</b>	<b>7,691.0</b>	<b>9,085.0</b>	<b>8,395.0</b>

Treasury Department, Division of Research and Statistics

October 19, 1938

\*Revised Budget Basis excludes the expenditures resulting from the operation of the Reconstruction Finance Corporation, the Commodity Credit Corporation and the Export-Import Bank.

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Treasury Department  
Division of Research and Statistics

Date... Nov. 16, ..... 19 39

To: Mr. McHugh

From: E. Kailey

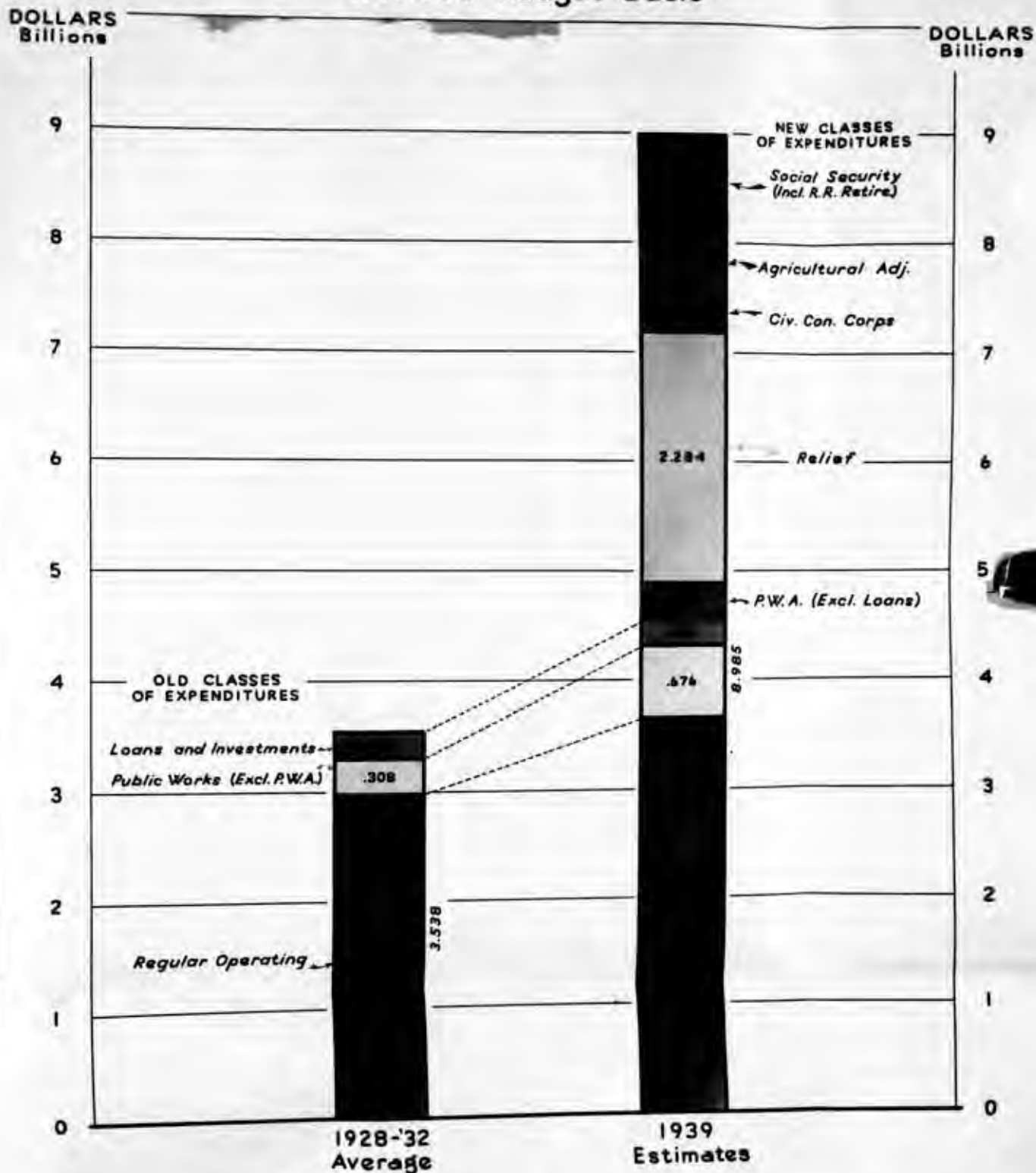
The three attached charts were sent to the Secretary on October 20, 1938, as attachments to a memorandum written to him entitled "The Government's Fiscal Problem".

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10/20/38

# COMPARISON OF 1939 EXPENDITURES WITH 1928-'32 AVERAGE\*

Revised Budget Basis†

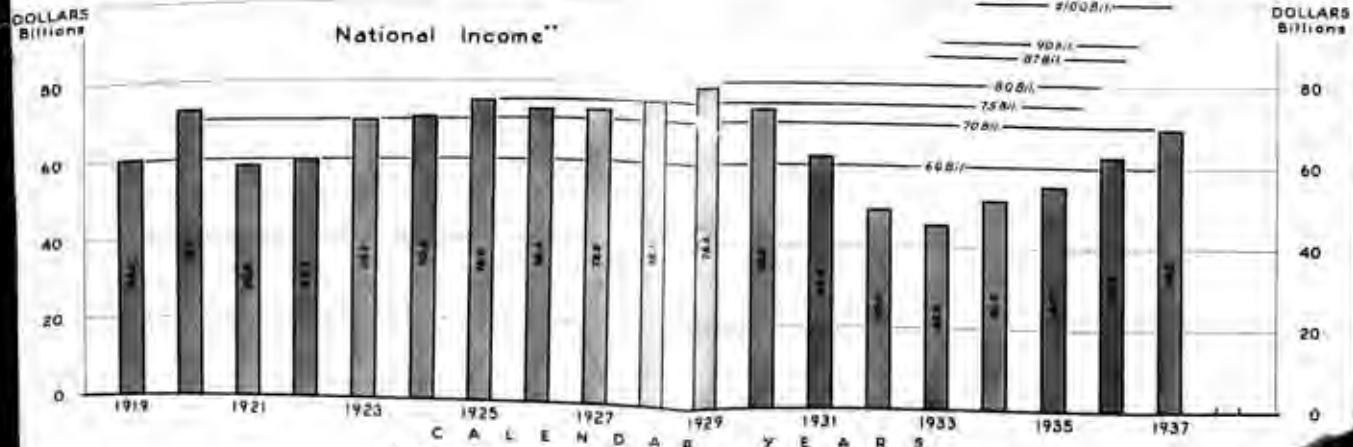
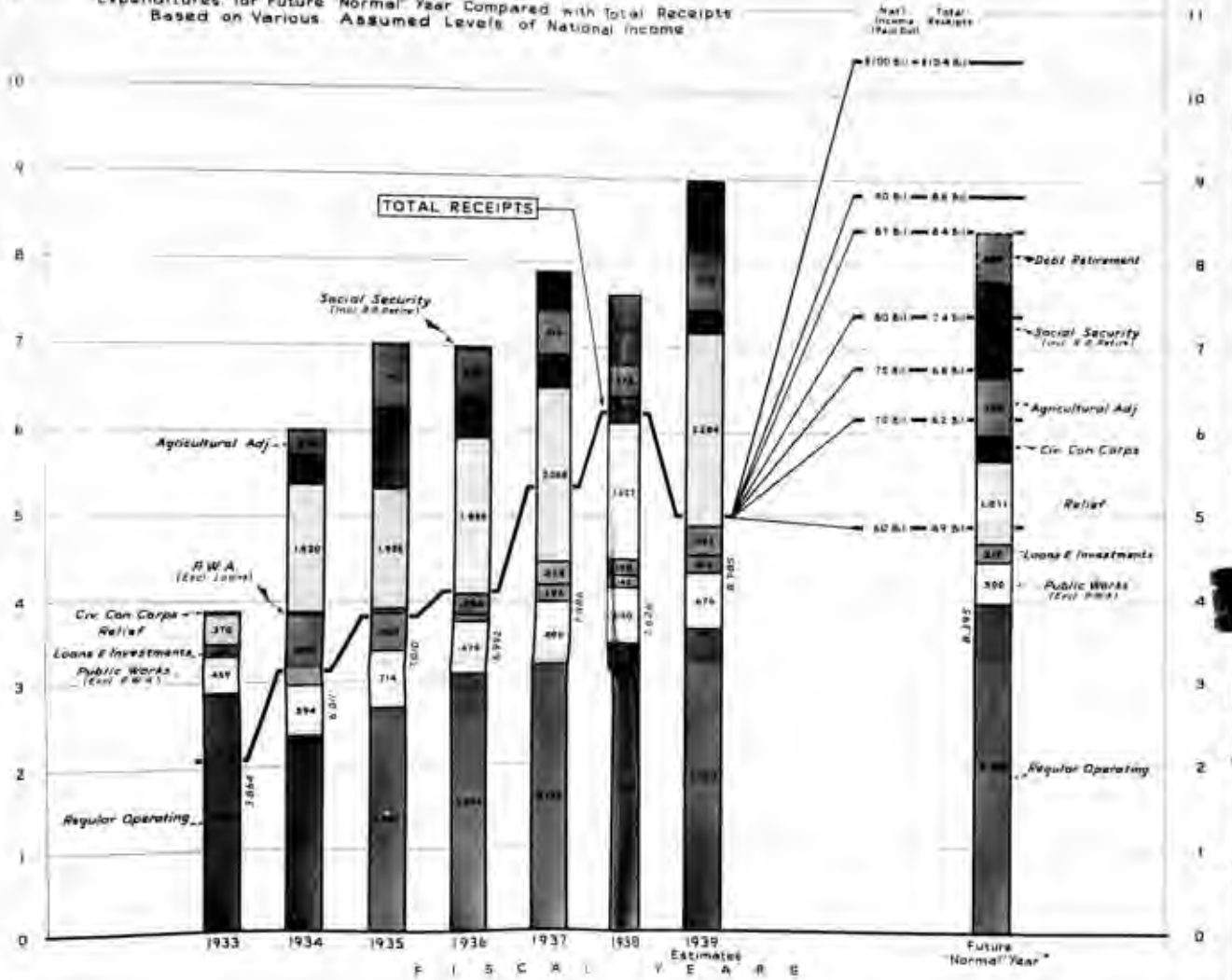


\* Excluding debt retirement.  
 † Excludes expenditures resulting from the operation of the Reconstruction Finance Corporation, Commodity Credit Corporation, and Export-Import Bank.

# FEDERAL EXPENDITURES<sup>1</sup> BY CLASSES, TOTAL RECEIPTS<sup>2</sup> AND NATIONAL INCOME<sup>3</sup>

## Expenditures<sup>1</sup> by Classes and Total Receipts<sup>2</sup> 1933-'39, and Future "Normal" Year<sup>4</sup>

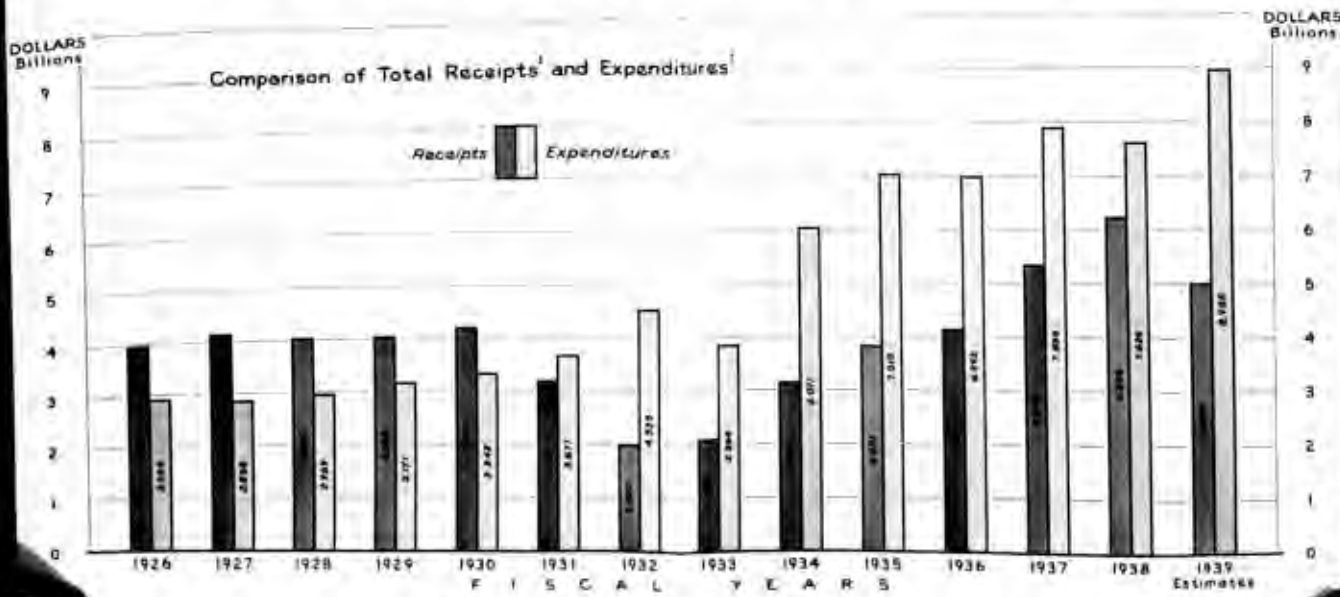
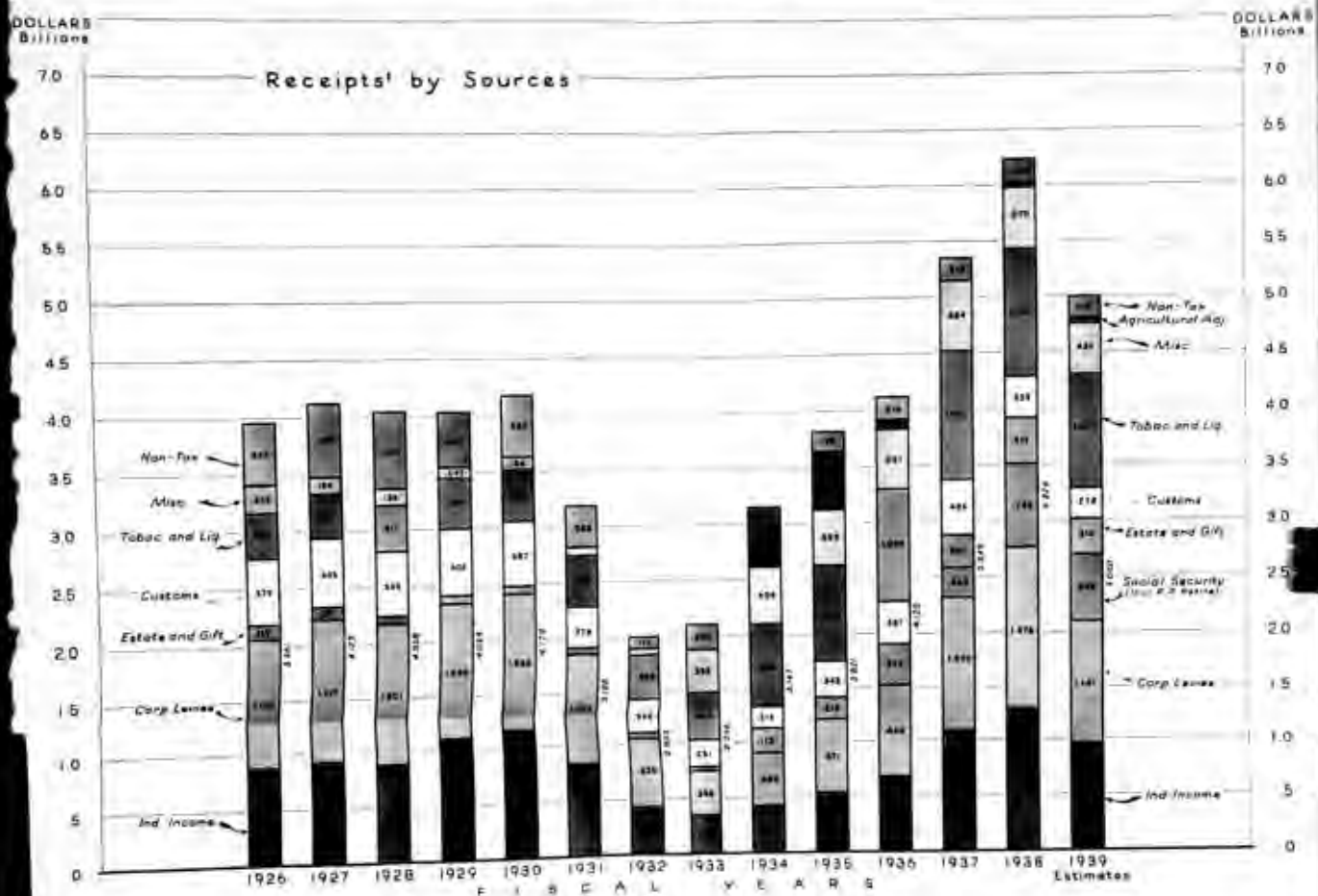
Expenditures for Future "Normal" Year Compared with Total Receipts Based on Various Assumed Levels of National Income



<sup>1</sup> Excludes public employment, and debt retirement except in future "normal" year. <sup>2</sup> Revised budget total; excludes expenditures resulting from restrictions of the Reconstruction Finance Corporation, Commodity Credit Corporation, and Export-Import Bank.  
<sup>3</sup> Custom and non-tax receipts on daily statement basis; all other on collection basis.  
<sup>4</sup> Future "normal" year assumes 1930 level for no pay and national retirement tax receipts and appropriations.  
<sup>5</sup> Census projection, 1919-'29; Income 1930 Est. Department.

# FEDERAL RECEIPTS BY SOURCES, AND TOTAL RECEIPTS AND EXPENDITURES

Fiscal Years 1926-'39



<sup>1</sup> Includes bank deposits and debt retirement. <sup>2</sup> Revised budget deficit; excludes expenditures resulting from operations of the Reconstruction Finance Corporation, Government Credit Corporation, and United States Bank.

<sup>3</sup> Customs and non-tax receipts (to date) strongly backfill (over) the estimated total.