DIARY

Book 564

August 29 - 31, 1942

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August 29, 1942

Telephone Conversation - Mr. Walton (Mr. Willkie's partner) and Mr. White
August 28, 1942 - 10:55 A. M.

Mr. Walton, partner of Mr. Willkie, telephoned Mr. White and said Mr. Willkie had left (presumably the country) and had asked Mr. Walton to keep Mr. White informed of negotiations with the British Treasury with respect to the release of motion picture industry blocked sterling. Mr. Walton said that Mr. Summerville was the British representative who was sent from London presumably to consider the matter. He had called on Mr. Willkie in his office on Tuesday, August 18 and told Mr. Willkie the final decision had to be made in London and they would have to wait word from there before they could give us any further advice.

Mr. Walton said Mr. Summerville had called him on Friday, August 28 and said it was his understanding that Mr. Willkie had been told by Phillips in Washington that they were certain the authorities in London were disposed to be most liberal and were ready to release all the funds or a great bulk of them. Mr. White asked whether Summerville had gone into the matter more with Walton. Mr. Walton replied he wasn't certain what Mr. Summerville was doing but he seemed to take the same reaction as Mr. Willkie and he was waiting to hear from London. Summerville said in view of wires, etc., he doubted whether they would hear before the end of next week, perhaps some time during the following week.

Mr. Walton said Summerville was planning to go to California. He added that Mr. Willkie seemed to think the whole affair was coming through and that he would keep Mr. White informed of any developments.

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THE COMMANDANT OF THE UNITED STATES COAST GUARD

WASHINGTON

29 August, 1942.

Dear Mr. Secretary:

I was pleased to read your compliment of August 26th upon the skill and efficiency of Lieutenant Commander Sinton and his crew during your inspection tour. Knowing that he and the others you mentioned will likewise derive pleasure in reading your comment, I am sending a copy of your letter to each of them.

Sincerely yours,

R R Waesche

R. R. WAESCHE
Vice Admiral, U.S. Coast Guard
Commandant

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

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MEMORANDUM

August 29, 1942.

TO: The Secretary

FROM: Mr. Sullivan

SUBJECT: Internal Revenue Bureau recruitment

JLS

From February 1st through July 31st the Internal Revenue Bureau has made 4,962 new appointments. Of this number, 1,775 were men and 3,187 were women.

During this same period, 196 women were promoted to positions formerly held by men. Twenty-two of these 196 are in specialized and technical positions.

It is the Commissioner's opinion that almost all of the 1,000 vacancies that existed three months ago have been filled and that the present vacancies have arisen since that time. He is going to send me a memorandum on this and I will advise you.

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UNITED STATES SAVINGS BONDS - SERIES E

Comparison of August sales to date with sales during the same number of business days in July and June 1942
(At issue price in thousands of dollars)

Date	August daily sales	Cumulative sales by business days: August	July	June	August as percent of July
ugust 1942					
1	$ 14,044	$ 14,044	$ 15,821	$ 19,834	88.8%
3	22,178	36,222	30,701	27,841	118.0
4	14,575	50,797	47,523	40,811	106.9
5	12,988	63,785	77,320	58,199	82.5
6	23,004	86,789	95,044	82,988	91.3
7	24,959	111,748	116,643	98,197	95.8
8	16,429	128,176	139,390	125,245	92.0
10	26,805	154,981	164,161	134,157	94.4
11	9,885	164,866	183,238	154,242	90.0
12	15,921	180,787	209,787	169,920	86.2
13	16,356	197,143	225,532	186,470	87.4
14	18,760	215,903	243,938	201,700	88.5
15	9,578	225,481	261,766	225,684	86.1
17	28,683	254,163	284,111	233,218	89.5
18	9,737	263,900	296,344	249,033	89.1
19	17,650	281,550	327,712	261,321	85.9
20	15,525	297,075	339,951	280,742	87.4
21	16,026	313,101	358,135	291,729	87.4
22	9,881	322,982	376,396	321,114	85.8
24	30,522	353,504	394,984	331,806	89.5
25	13,692	367,195	405,679	347,673	90.5
26	16,107	383,303	438,256	362,550	87.5
27	14,932	398,234	455,706	378,505	87.4
28	17,328	415,563	473,962	392,224	87.7

fice of the Secretary of the Treasury,
Division of Research and Statistics.

August 29, 1942.

urce: All figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds.

Note: Figures have been rounded to nearest thousand and will not necessarily add to totals.

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UNITED STATES SAVINGS BONDS - SERIES F AND G COMBINED

Comparison of August sales to date with sales during the same number of business days in July and June 1942
(At issue price in thousands of dollars)

Date	August daily sales	Cumulative sales by business days: August	July	June	August as percent of July
August 1942					
1	$ 12,222	$ 12,222	$ 12,597	$ 9,705	97.0%
3	16,587	28,810	21,986	17,601	131.0
4	12,448	41,258	32,441	26,235	127.2
5	12,847	54,105	49,175	40,009	110.0
6	17,447	71,552	62,561	49,353	114.4
7	13,225	84,777	84,413	55,888	100.4
8	7,789	92,566	101,585	67,414	91.1
10	14,216	106,782	124,568	72,366	85.7
11	5,389	112,171	141,618	82,310	79.2
12	8,803	120,974	162,232	89,852	74.6
13	6,401	127,375	176,590	95,254	72.1
14	9,744	137,119	191,991	101,464	71.4
15	3,253	140,372	205,833	108,715	68.2
17	13,124	153,496	221,147	112,279	69.4
18	4,814	158,309	230,842	119,749	68.6
19	10,106	168,415	252,731	126,048	66.6
20	8,266	176,681	262,178	134,062	67.4
21	6,161	182,842	278,505	137,429	65.7
22	3,365	186,207	293,679	147,698	63.4
24	10,507	196,715	308,077	153,532	63.9
25	5,975	202,690	316,893	162,774	64.0
26	9,278	211,968	338,137	170,547	62.7
27	8,343	220,311	350,522	176,410	62.9
28	6,532	226,844	365,305	183,433	62.1

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

August 29, 1942.

Source: All figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds.

Note: Figures have been rounded to nearest thousand and will not necessarily add to totals.

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UNITED STATES SAVINGS BONDS - TOTAL

Comparison of August sales to date with sales during the same number of business days in July and June 1942
(At issue price in thousands of dollars)

Date	August daily sales	Cumulative sales by business days			
		August	July	June	August as percent of July
ugust 1942					
1	$ 26,267	$ 26,267	$ 28,418	$ 29,539	92.4%
3	38,765	65,032	52,687	45,442	123.4
4	27,023	92,055	79,964	67,046	115.1
5	25,835	117,890	126,495	98,208	93.2
6	40,450	158,341	157,605	132,341	100.5
7	38,184	196,524	201,056	154,085	97.7
8	24,218	220,742	240,974	192,659	91.6
10	41,021	261,763	288,729	206,523	90.7
11	15,274	277,037	324,856	236,552	85.3
12	24,724	301,761	372,020	259,772	81.1
13	22,757	324,518	402,122	281,724	80.7
14	28,504	353,022	435,929	303,163	81.0
15	12,830	365,852	467,599	334,398	78.2
17	41,806	407,659	505,257	345,497	80.7
18	14,551	422,209	527,186	368,782	80.1
19	27,756	449,965	580,443	387,369	77.5
20	23,791	473,756	602,129	414,804	78.7
21	22,187	495,943	636,640	429,158	77.9
22	13,246	509,189	670,075	468,812	76.0
24	41,029	550,219	703,062	485,338	78.3
25	19,667	569,885	722,572	510,446	78.9
26	25,385	595,271	776,393	533,097	76.7
27	23,275	618,546	806,228	554,915	76.7
28	23,861	642,406	839,266	575,657	76.5

ffice of the Secretary of the Treasury,
Division of Research and Statistics.

August 29, 1942.

urce: All figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds.
Note: Figures have been rounded to nearest thousand and will not necessarily add to totals.

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Sales of United States savings bonds
August 1 through August 28, 1942
Compared with sales quota for same period
(At issue price in millions of dollars)

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Date	Series E				Series F and G				Total			
	Actual sales		Quota, August 1 to date	Sales to date as % of quota	Actual sales		Quota, August 1 to date	Sales to date as % of quota	Actual sales		Quota, August 1 to date	Sales to date as % of quota
	Daily	August 1 to date			Daily	August 1 to date			Daily	August 1 to date		
1	$ 14.0	$ 14.0	$ 16.0	87.5%	$ 12.2	$ 12.2	$ 7.7	158.4%	$ 26.3	$ 26.3	$ 23.7	111.0%
3	22.2	36.2	47.3	76.5	16.6	28.8	21.5	134.0	38.8	65.0	68.8	94.5
4	14.6	50.8	61.0	83.3	12.4	41.3	29.6	139.5	27.0	92.1	90.6	101.7
5	13.0	63.8	84.0	76.0	12.8	54.1	45.4	119.2	25.8	117.9	129.4	91.1
6	23.0	86.8	107.3	80.9	17.4	71.6	58.7	122.0	40.5	158.3	166.0	95.4
7	25.0	111.7	134.4	83.1	13.2	84.8	68.8	123.3	38.2	196.5	203.2	96.7
8	16.4	128.2	154.1	83.2	7.8	92.6	76.3	121.4	24.2	220.7	230.4	95.8
10	26.8	155.0	190.6	81.3	14.2	106.8	87.9	121.5	41.0	261.8	278.5	94.0
11	9.9	164.9	205.1	80.4	5.4	112.2	94.1	119.2	15.3	277.0	299.2	92.6
12	15.9	180.8	227.1	79.6	8.8	121.0	105.1	115.1	24.7	301.8	332.2	90.8
13	16.4	197.1	247.9	79.5	6.4	127.4	114.0	111.8	22.8	324.5	361.9	89.7
14	18.8	215.9	271.0	79.7	9.7	137.1	120.9	113.4	28.5	353.0	391.9	90.1
15	9.6	225.5	287.7	78.4	3.3	140.4	126.4	111.1	12.8	365.9	414.1	88.4
17	28.7	254.2	319.2	79.6	13.1	153.5	135.8	113.0	41.8	407.7	455.0	89.6
18	9.7	263.9	332.2	79.4	4.8	158.3	141.3	112.0	14.6	422.2	473.5	89.2
19	17.6	281.6	353.0	79.8	10.1	168.4	151.9	110.9	27.8	450.0	504.9	89.1
20	15.5	297.1	373.6	79.5	8.3	176.7	161.0	109.8	23.8	473.8	534.6	88.6
21	16.0	313.1	397.4	78.8	6.2	182.8	168.3	108.6	22.2	495.9	565.7	87.7
22	9.9	323.0	415.1	77.8	3.4	186.2	174.3	106.8	13.2	509.2	589.4	86.4
24	30.5	353.5	449.0	78.7	10.5	196.7	184.8	106.4	41.0	550.2	633.8	86.8
25	13.7	367.2	462.9	79.3	6.0	202.7	191.0	106.1	19.7	569.9	653.9	87.2
26	16.1	383.3	484.5	79.1	9.3	212.0	203.0	104.4	25.4	595.3	687.5	86.6
27	14.9	398.2	505.0	78.9	8.3	220.3	213.2	103.3	23.3	618.5	718.2	86.1
28	17.3	415.6	527.8	78.7	6.5	226.8	221.4	102.4	23.9	642.4	749.2	85.7
29			544.2				228.1				772.3	
31			575.0				240.0				815.0	

ice of the Secretary of the Treasury, Division of Research and Statistics. August 29, 1942.

rce: Actual sales figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds. Figures have been rounded and will not necessarily add to totals.

ote: Quota takes into account both the daily trend during the week and the monthly trend during the month.

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE AUG 29 1942

TO Secretary Morgenthau

FROM Randolph Paul

Attached is a letter from the Secretary of War setting forth the arrangement for the allocation of 6,000 tons of "free" silver to the War Department. Upon approval by you, this letter will serve as the basis for carrying out the arrangement.

There are also attached a letter from the Secretary of War explaining to you that the nature of the use to which this silver will be put is secret and a letter from Donald Nelson requesting that this use be given the highest priority.

Since the agreement is between two Cabinet officers who are acting on behalf of the United States, you are not indemnified against loss in the technical sense in which you were indemnified by the Defense Plant Corporation and the Reconstruction Finance Corporation. However, the War Department does state that it will return the identical silver or an equivalent amount. The silver will be closely guarded by military forces and the title to the silver will remain as at present.

I am satisfied that you have legal authority to enter into such an arrangement. Your authority in this case seems even clearer than your authority to enter into the contract with the Defense Plant Corporation. In view of the Attorney General's opinion of last spring, I believe that there is no need to clear this arrangement with him.

In April the President approved your making "free" silver available to Government- or privately-owned war plants. The scope of that approval is broad enough to include this arrangement with the War Department.

REP.

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WAR PRODUCTION BOARD
WASHINGTON, D. C.

OFFICE OF
[DON]ALD M. NELSON
CHAIRMAN

August 28, 1942

The Honorable,

The Secretary of the Treasury.

Dear Mr. Secretary:

The War Department has discussed with me the allocation to it of 6,000 tons of silver for use as a substitute for copper. I am familiar with the uses for which such silver is desired and feel that this use must be given the highest priority. I recommend that the Treasury make appropriate arrangements to transfer this quantity of silver to the War Department out of the "free" silver stocks in the Treasury.

I shall take any necessary steps to advise the Defense Plant Corporation of this allocation of the "free" silver stocks so that any proper changes can be made in its program for use of "free" silver in lieu of other strategic materials.

Very truly yours,

D. M. Nelson

Donald M. Nelson

SECRET

VICTORY
BUY
UNITED STATES
WAR
BONDS
AND
STAMPS

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SECRET

WAR DEPARTMENT
WASHINGTON

AUG 29 1942

The Honorable,

The Secretary of the Treasury.

Dear Mr. Secretary:

In connection with my letter to you of today requesting the transfer of custody of 6,000 tons of silver to the War Department to be used as a substitute for copper, may I advise you that the important project, the use for which this silver is desired, is a highly secret matter. At this time the interests of the Government do not permit my disclosing the nature of the use.

The silver is desired for use on property which will be Government-owned, it will be adequately guarded at all times, and the use is of such a nature that the silver will not be consumed and will be available for return at the expiration of the use.

The use of the silver which is contemplated not only will relieve a substantial amount of other critical materials for use in the war effort but is in itself of the utmost importance to the prosecution of the war.

Sincerely,

Henry L Stimson

Secretary of War.

SECRET

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WAR DEPARTMENT
WASHINGTON

AUG 29 1942

The Honorable,

The Secretary of the Treasury.

Dear Mr. Secretary:

In an effort to conserve critical materials and at the same time expedite construction of a war project, the Manhattan District of the Corps of Engineers requires 6,000 tons of silver to be used as a substitute for copper in the construction of that project. It is understood that the Treasury has available a quantity of silver adequate for the needs of the war project.

Representatives of the Chief of Engineers have discussed the use of this silver with Mr. D. W. Bell, Under Secretary of the Treasury, who has advised that the transfer proposed herein is in general accord with the procedure recently followed by the Defense Plant Corporation and the Reconstruction Finance Corporation in their agreements with the Treasury effecting the similar use of a large tonnage of silver. At the request of the Treasury Department, the War Department has obtained clearance for the tonnage required from the War Production Board and the Army and Navy Munitions Board.

Accordingly, I request that the Treasury transfer to the War Department custody of certain silver now held by the Treasury, upon the following terms and conditions:

(1) The Treasury will at any time up to [illegible], 1944, deliver to the War Department, upon the latter's request, for uses in accordance with the purposes [illegible] in this letter, silver containing [illegible] 175,000,000 fine troy ounces [illegible] of silver deemed by the Secretary of the Treasury to be unoccupied and unproductive and [illegible] for [illegible] connected with the monetary [illegible] (such silver to the extent available [illegible] bars .999 fine), at such places where [illegible] held, at such times, and in such quantities, as the War Department may from time to time request by [illegible] signed by the District Engineer, Manhattan District, Corps of Engineers, such delivery to be made against receipts therefor duly executed by the District Engineer, Manhattan District, Corps of Engineers.

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(2) At all times, regardless of the person in whose possession such silver shall be, title thereto shall be and remain, as it now is, in the United States.

(3) Any silver received by the War Department will be returned in the quantity, form and fineness in which and to the place from which it was received. The silver shall be so returned upon the expiration of five (5) years from the date of the receipt of such silver by the War Department, or upon written notice by the Secretary of the Treasury to the effect that the redelivery of any part, or all, of such silver is necessary for reasons connected with the monetary requirements of the United States or upon the termination of the arrangement described herein for any other cause whether or not specifically stated herein, whichever of the foregoing events shall first happen. The War Department will return the identical silver received by it to the place from which it received the silver, and if such silver is not redelivered, silver of the equivalent quantity, form and fineness will be delivered to the place from which the War Department received the silver.

(4) [illegible] plants [illegible] Department, [illegible] utility [illegible] effort [illegible] are [illegible] or [illegible].

HMS

[illegible]

[illegible]

[illegible]

Ltr. to the Secretary of the Treasury (Cont'd)

c. Upon request of the Treasury, will make appropriate reports respecting the silver, consistent with the purposes of this arrangement, and also will make periodic inventories of the silver and communicate the results to the Treasury.

d. Assure that in the event that provision is made for the acquisition or lease to any plant, or any part of any plant, where such silver is installed, by any private person, the title of the United States to such silver shall be fully protected.

(6) The War Department will assume all expense, risk of loss and obligations arising out of, or in connection with the delivery, redelivery, transportation, fabrication, installation or maintenance of such silver.

If the arrangement described in this letter meets with your approval, it is requested that you indicate your approval by signing this letter and one of the copies, in the place provided at the foot hereof, and returning the copy so approved to me.

Sincerely yours,

Henry L Stimson

Secretary of War.

Approved: August 29, 1942

Daniel W. Bell

Acting Secretary of the Treasury.

SECRET

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14

Treasury Department
Division of Monetary Research

Date August 29, 1942

To: Miss Chauncey

From: Mr. White

The Secretary might be interested in looking at the attached report on Canada's U. S. Dollar Position.

MR. WHITE
Branch 2058 - Room 214½

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Treasury Department
Division of Monetary Researc

Date August 29 1942

o: Miss Chauncey

m: Mr. White

The Secretary might be interested

glancing at the attached report on

ada's U. S. Dollar Position.

MR. WHITE
Branch 2058 - Room 214½

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CANADA'S U. S. DOLLAR POSITION

Division of Monetary Research

U. S. Treasury Department

STRICTLY CONFIDENTIAL

August, 1942.

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The following study of Canada's international financial position was prepared by T. M. Kistler of the Division of Monetary Research. It brings up-to-date the report completed by the Treasury last April.

The Treasury Department estimated in July that Canada will end the year 1942 with a gold and U. S. dollar reserve of $350-$500 million. The Canadian Government, however, is not so optimistic. It predicts that Canada's official holdings of gold and U. S. dollars at the close of this year will amount to $271 million.

Carrying its forecast forward, the Canadian Government tentatively estimates that Canada will increase its official U. S. dollar holdings by $51 million during the first quarter of next year to reach a total of $322 million on March 31, 1943. These figures for the first three months of 1943 are necessarily rough and only tentative, because of the large number of unknown factors in the picture, but they serve to indicate the probable trend.

The current Canadian forecast, although less optimistic than the Treasury's estimates, indicates continued improvement in Canada's U. S. dollar position during the next half year or so. The figures submitted by the Canadian Ministry of Finance allow for a maximum probable increase in Canada's official U. S. dollar resources during the last six months of 1942 of $27 million, whereas the Treasury forecast a minimum probable increase during this period of $100 million.

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The divergence between these two estimates stems largely from three sources:

First, "Hyde Park" exports. Despite the increase of roughly $500 million in U. S. Government contracts placed in Canada since the completion of the March forecast, the Canadian Government raised its estimate of receipts from these contracts, for the period, July through December 1942, by only $30 million. The U. S. Treasury, on the other hand, allowed for a rise of $100 million to $150 million above the Canadian Government's earlier estimate. This expected increase was based on a schedule of receipts from U. S. Government contracts with War Supplies, Ltd., drawn up by the Department of Munitions and Supplies as of May 31, 1942, and on a projection of the recent trend of Canada's receipts from special materials deals made with Metals Reserve Corporation.

Secondly, capital imports from the United States. The U. S. Treasury estimate was based on the assumption that the unexpectedly large inflow of capital from the United States to Canada which occurred during the first six months of 1942, would continue in about the same volume during the remainder of this year. The Canadian Ministry of Finance, on the other hand, disturbed by the preponderance in these transactions of bonds with a foreign payment feature, advises that it is seriously considering taking steps to reduce this capital inflow and doubts that it will permit the inflow during the remainder of this year to reach anything like the magni-

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tude of the first six months. Unexpected receipts from capital imports from the United States, January through June 1942, accounted for almost one-half of the $124 million discrepancy between the Canadian-forecast and the actual change in Canada's U. S. dollar holdings, January 1 to June 30, 1942. The Canadian Government's latest forecast allows for a $20 million rise in capital imports from the United States, July through December 1942, above what they expected last March.

Thirdly, current U. S. dollar expenditures and receipts. As with capital transactions, the U. S. Treasury assumed that the Canadian Government's March forecast for the last six months of 1942, overstated Canada's needs for U. S. dollars on current account, outside the Hyde Park Agreement, by roughly the same amount as the companion estimate for the first six months had done--that is, overstated them by $40 million. The Canadian Government, however, now places its deficit of U. S. dollars for goods and services, July through December 1942, at a figure $10 million higher than it did last March.

H. D. White,
Director of Division of
Monetary Research

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CANADA'S U. S. DOLLAR POSITION

Report prepared by

T. M. Kistler

Division of Monetary Research,
U. S. Treasury Department

August, 1942.

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CANADA'S U. S. DOLLAR POSITION

The Canadian Ministry of Finance on July 27, 1942, submitted a memorandum to the U. S. Treasury which contains both a reconciliation of the actual with the Canadian-forecast change in Canada's U. S. dollar position, January 1 to June 30, 1942, and a revised estimate of Canada's U. S. dollar expenditures and receipts for the nine months ending March 31, 1943. This document has provided the data necessary for the detailed revision of the Treasury's study of Canada's U. S. dollar position which is set forth in the following pages. Figures used are expressed in terms of U. S. dollars unless otherwise indicated.

I. SUMMARY

Contrary to the Canadian Government's forecast last March, Canada's official gold and U. S. dollar reserves have increased so far in 1942, from $188 million on January 1 to $244 million on July 1. (Details of Canada's holdings of U. S. dollar exchange assets are given in Section II, pp. 4-10.)

This favorable trend is expected to continue at least through the first quarter of 1943. The current Canadian Government forecast indicates a further rise in official Canadian gold and U. S. dollar holdings of $27 million, or to $271 million, by December 31, 1942, and of an additional $51 million, or to $322 million, by the close of March 31, 1943.

These expected accretions of $27 million and $51 million, respectively, represent the anticipated balance of U. S. dollar inpayments to be made to Canada during each of these two periods. This balance is derived from the estimates shown on the next page.

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	July thru Dec. 1942	Jan. thru March 1943
	(Millions U. S. $)	
1. Canada's need for U.S. dollars to meet its excess of U.S. dollar obligations over current receipts from exports of merchandise and services, exclusive of "Hyde Park" and gold exports.................................... (See Section III, pp. 11-31, for component estimates.)	393	175
2. Means available to Canada of meeting this need for U.S. dollars:		
a. Sale of newly-mined gold.......................... (See Section IV, pp. 32-35, for data on Canada's production and sale of gold.)	62	20
b. Sale of securities and other assets to U.S. (gross).................................... (See Section V, pp. 36-41, for details of transfers of private capital between the U.S. and Canada.)	59	32
c. Exports on U.S. Government orders placed in Canada pursuant to the Hyde Park Declaration (gross)............................. (See Section VI, pp. 42-51, for further information on Hyde Park transactions.)	299	174
Total U.S. dollar receipts expected from these sources to be available to Canada to meet its U.S. dollar needs...............	420	226
3. Surplus of U.S. dollar receipts over payments to be added to Canada's official holdings of gold and U.S. dollars..........................	27	51

These figures represent probable maxima in the opinion of the Canadian Ministry of Finance; it predicts that the actual increase in Canada's holdings of U. S. dollar resources is not likely to be nearly so large as the above estimates. In the document submitted to the Treasury on July 27, 1942, it is pointed out that these forecasts make allowance for only those changes in current trends which can be estimated with a reasonable degree of accuracy and that there are at least two, and possibly three, unfavorable factors, which may reduce Canada's net receipts of U. S. dollars during the next few months but, which because of their uncertainty had to be ignored, at least in part, in compiling the figures shown above.

First, Canada's import of capital from the United States may be sharply curtailed in the near future. This will almost certainly be the case if the Dominion Government, as it is considering doing, places an embargo on the export of Canadian securities to this country. Sales of such securities account for two-thirds of the unusually large gross inflow of American capital to Canada, January through June 1942. A prohibition on their export would, the Canadian Ministry of Finance believes, reduce Canada's net U. S. dollar receipts during the current period by as much as $35 million.

Secondly, further shortages of U. S. materials would reduce Canadian expenditures in this country, but they would lower Canada's receipts from exports much more. The possible effect of such a development on Canada's U. S. dollar position, is impossible to estimate at the present time. The Canadian Ministry of Finance ventures the prediction that it might wipe out much of the rest of the estimated increase in Canada's U. S. dollar holdings through March 31, 1943.

Thirdly, there is a possibility that temporary capital advances made on dividend and merchandise account by Americans to Canadians have risen during recent months and that they may be drawn down during the next half year or so. The Canadian Ministry of Finance believes that when imports have been increasing rapidly, as in the immediate past, there may be a delay in paying for them which results in a current, but purely temporary, addition to Canada's exchange resources. It further points out that there is evidence that purchases of exchange for the transfer of earnings on American capital invested in Canada are lagging behind the actual earnings themselves. Both developments may be due to the generally widespread expectation in Canada of an imminent return of the Canadian dollar to par. If transfers of payments on merchandise and service account have been being postponed during recent months on the hope of reaping an exchange gain, the demand for U. S. dollars in the immediate future may exceed the Canadian Government's current estimates, thereby reducing the figure for net U. S. dollar receipts through March 1943.

If, however, American exports of capital to Canada continue at the level of the first half of 1942, and if, further, the Canadian Government's estimate of delivery schedules on U. S. Government orders proves to be unduly pessimistic, then Canada's net acquisition of U. S. dollars, July 1942 through March 1943, may exceed current Canadian expectations.

This is what seems to be occurring so far this quarter. Funds held by the Canadian Government with the Federal Reserve Bank of New York were $12 million higher on August 8 than on July 1. This increase is three-fourths as much as the Canadian Government forecast would be added to Canada's official U. S. dollar reserves during the three months, July through September 1942.

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II. CANADA'S U. S. DOLLAR ASSET POSITION

A. "Official" reserves held by the Canadian Government

On July 1, 1942, the Canadian Government held $244 million of gold and U. S. dollars, as follows:

	(Millions U. S. $)
Gold........................	125
U. S. dollar balances.........	119
Total....................	244

The $119 million of U. S. dollar balances is the amount of Canadian-owned funds in the United States, reported by the Canadian Ministry of Finance as available to the Canadian Government on July 1, 1942. It is the total of balances held in this country by the Canadian Ministry of Finance, the Bank of Canada and the Canadian Foreign Exchange Control Board. The inclusion of deposits of the Foreign Exchange Control Board largely accounts for the $27 million discrepancy between the above Canadian-reported figure of $119 million, for "official" Canadian funds in the United States on July 1, 1942, and $92 million, the amount reported for the same date in U. S. Treasury capital movements data as held in this country by the Canadian Government for the account of Canada.

The above figure of Canada's "official" holdings of U. S. dollars does not include $163 million held by the Canadian Government on deposit with the Federal Reserve Bank of New York for the account of France. This is the total of repayments made by the British to the French Government on French contracts taken over by the British in June 1940.

B. Other Canadian assets in the United States

In addition to these "official" reserves held by the Dominion Government, Canadian individuals and concerns hold a total of roughly $750 million of U. S. assets. They are comprised of:

	(Millions U. S. $)
Private U. S. dollar balances..	170
U. S. securities..............	250
Direct investments in U.S......	330
Total.....................	750

Private U. S. dollar balances. The above figure of $170 million for private Canadian funds in this country is $27 million lower than the amount reported in U. S. Treasury capital movements data, upon which it is based. The U. S. Treasury figure has been reduced for the purpose at hand to offset the inclusion above, in so-called "official" funds, of the deposits of the Canadian Foreign Exchange Control Board. Canadian "private" funds in the New York Federal Reserve District totalled $173 million on July 1, 1942, and Canadian "private" deposits outside the New York Federal Reserve District aggregated $24 million on July 1, 1942, the latest date for which we have data.

In the opinion of Canadian Government officials, these private balances are at minimum working levels and are, therefore, unavailable to the Canadian Government. They estimate that Canadian individuals and concerns other than banks and insurance companies, hold $20 million of U. S. dollar balances and they assume, for purposes of forecasting Canada's U. S. dollar position, that the sum of these balances does not vary over time. Presumably the remainder of the Canadian-owned funds in the United States are held by Canadian financial institutions against their U. S. dollar liabilities.

Changes in the amount of "private" Canadian balances held in the United States since the outbreak of war, as reported in U. S. Treasury capital movements data, are shown below on p. 9.

U. S. securities. The estimate of $250 million for Canadian-held U. S. securities is the Canadian figure adjusted for net sales. The Ministry of Finance estimates, on the basis of a compulsory registration at the beginning of the war, that Canadian residents, other than banks and insurance companies, held $280 million of U. S. securities as of December 31, 1940. It estimates further that during the following year and a half, Canadians sold $67 million of privately-held U. S. dollar assets. Of this amount, according to data published by the Dominion Bureau of Statistics, something over $20 million represents net sales of U. S. securities. This is almost $10 million lower than the net movement shown in U. S. Treasury capital movements figures.

In addition, Canadian insurance companies hold about $480 million and Canadian banks about $40 million of U. S. securities. These figures are as submitted to us by the Canadian Government and reflect the position of these institutions as of September 30 and December 31, 1940, respectively. These are the latest dates for which we have information. It is believed, however, that there has not been any substantial change in the aggregate size of these holdings since the latter part of 1940.

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The above estimate of $250 million for Canadian holdings of U. S. securities is considerably lower than that of the Department of Commerce. The Department of Commerce estimates that as of December 31, 1940, Canadians held about $440 million of U. S. securities. Reducing this figure by $30 million, the amount of net sales of U. S. securities by Canada to the United States, January 1, 1941 to June 24, 1942, reported in U. S. Treasury capital movements data, we arrive at an estimate for current Canadian holdings of $410 million. The principal reason for the large discrepancy between the two estimates appears to be that the Department of Commerce included, and the Canadian Government excluded, U. S. securities held by non-resident-owned Canadian companies.

<u>Direct investments in the United States</u>. The Dominion Bureau of Statistics estimates that, as of December 31, 1938, Canadian direct investments in this country had a book value of about $330 million. Of this amount, over $200 million represents investments of Canadian railways in lines in the United States, many of which are of doubtful marketable value.

The Department of Commerce estimates the book value of Canadian direct investments in the United States as of December 31, 1940, to be about $480 million. As in the case of the security estimates, the discrepancy between the Department of Commerce figure and that of the Canadian Government appears to be due largely to the inclusion in the former, and the exclusion from the latter, of the holdings in the United States of a number of companies incorporated in Canada but owned by non-residents of Canada.

In addition to Canada's U. S. security holdings and Canadian direct investments in the United States, the Department of Commerce estimates that, as of December 31, 1940, Canadians held miscellaneous investments in the United States with an aggregate value of $78 million. These investments are comprised of trust funds established on behalf of Canadian beneficiaries, estates with Canadian legatees, real estate mortgages, unincorporated real estate, oil and gas royalties, and miscellaneous interests. The estimated value is based upon capitalized income. The Dominion Bureau of Statistics has reported no comparable category of Canadian-owned U. S. assets.

C. <u>Canada's liquidation of U. S. dollar assets, September 1939 through June 1942</u>

The Canadian Government, at the outbreak of war, held U. S. dollar exchange resources totalling $261 million, as follows:

	(Millions U. S. $)
Gold....................................	205
U. S. dollar balances..................	56

By January 1, 1941, as a result of its requisitioning $156 million of private Canadian balances held in the United States, the Canadian Government's holdings of gold and U. S. dollars had risen $69 million, or to a total of $330 million. These holdings were comprised of:

	(Millions U. S. $)
Gold....................................	136
U. S. dollar balances..................	194

The year 1941 saw the heaviest drain on Canada's U. S. dollar resources since the outbreak of the war. The Canadian Government sold no gold out of its reserves during the year, but met Canada's deficit of U. S. dollars by drawing down its balances in the United States. They fell from $194 million on January 1, 1941, to $52 million at the close of the year. Approximately half, or $67 million, of this decline in Canada's official U. S. dollar balances was recovered during the first six months of 1942. This recovery reflected primarily a marked improvement in Canada's U. S. dollar position, but $11 million of the increase was due to the sale of gold from the Government's reserves. To this extent, the increase in official balances so far in 1942 represents merely a change in the composition of, and not a net addition to, the Canadian holdings of liquid U. S. dollar assets.

In addition to the reduction of $173 million in the amount of liquid U. S. dollar resources available to the Dominion Government, Canadian individuals and concerns sold a total of $148 million of U. S. securities and other U. S. assets during the period, September 15, 1939 to June 30, 1942, bringing the total decline in Canada's U. S. dollar assets since the outbreak of war to $321 million. The drain by principal categories of assets is summarized in the table below:

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Decrease (-) or Increase in Canada's Holdings of U. S. Dollar Assets, September 15, 1939 through June 30, 1942

	Sept. 15, 1939-Dec. 31, 1940	Jan. thru Dec. 1941	Jan. thru June 1942	Total thru June 1942
	(Millions U. S. $)			
Gold..............	- 69	—	- 11	- 80
"Official" U.S. dollar balances.	138	-142	67	63
"Private" U.S. balances.........				
Banks..........	- 26	—	—	- 26
Individuals and concerns......	-130	—	—	-130
U.S. securities and other U.S. assets.	- 81	- 40	- 27	-148
Total drain on Canada's U.S. dollar assets....	-168	-182	29	-321

The above reported drain of $321 million is $26 million higher than that shown in the Canadian documents submitted to the U. S. Treasury on March 18 and July 27, 1942. The discrepancy arises from the fact that the above figure includes, and the tabulations submitted by the Canadian Government excludes, a $26-million reduction in U. S. dollar balances held by Canadian banks, which the Canadian Ministry of Finance in July 1941 reported had been effected during the first year of war.

In addition to the decline of $321 million in Canada's pre-war holdings of U. S. dollar exchange assets, the Canadian Government has sold to the U. S. Treasury $225 million of gold received from the United Kingdom, September 1939 through December 1940, in settlement of Canada's favorable balance of payments with the Sterling Area. See below Section VII, pp. 52-57 for a discussion of Canada's balance of payments with the Sterling Area since the outbreak of war.

Canada's holdings of U. S. dollar balances on various dates since September 1939, are set forth in the table below which gives both the Canadian-reported figures of "official" holdings of U. S. dollars, and U. S. Treasury capital movements data on Canadian short-term banking funds in the United States. The discrepancy

between the two sets of figures for "official" funds is due partly to a difference in reporting dates and partly to a difference in coverage. Deposits of the Canadian Foreign Exchange Control Board are included in "official" funds in the Canadian figures, while they are treated as "private" in U. S. Treasury data. We believe, however, that these deposits do not fluctuate widely and we think that this is indicated by the fact that during the past year and a half the differential between the two series of figures on "official" balances has varied by only $10 million for those dates for which we have data.

	Canadian "official" funds in U. S. (as reported by the Canadian Government)	Canadian short-term funds in U.S. (as reported in U.S. Treasury data on nearest reporting dates): Official funds, held for account of Canada	Private funds
	(Millions U. S. $)		
1939			
Sept. 15........	56	52	274
Dec. 31........		59	215
1940			
Mar. 31........		43	208
June 30........		88	171
Sept. 30........		177	179
Dec. 31........	194	170	154
1941			
Mar. 31........	141	107	163
June 30........	119	88	167
Sept. 30........	122	89	186
Dec. 30........	52	25	185
1942			
Mar. 31........	104	74	188
June 30........	119	92	196

With the possible exception of the figure reported in U. S. Treasury data for June 30, 1940, the above figures do not include deposits held by the Canadian Government with the Federal Reserve Bank of New York for the account of France. These deposits represent repayments of advances by the British to the French on French contracts taken over in June 1940. The funds so held by the Canadian Government rose from $55 million on September 25, 1940, to $163 million at the close of May 1941. No repayments have since been made.

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D. Canadian-expected increase in Canada's U. S. dollar assets July 1942 through March 1943

The Canadian Ministry of Finance expects Canada to add to its holdings of U. S. dollar exchange assets during the nine months ending March 31, 1943. Roughly half of the forecast $27 million increase in the Canadian Government's U. S. dollar balances during the last six months of 1942, and over 10 percent of the anticipated $51 million rise during the first quarter of 1943, are expected to be offset by the sale of other Canadian-owned U. S. dollar assets, estimated at the rate of $7 million quarterly for the next nine months. The present Canadian forecast of changes in Canada's holdings of U. S. dollar assets during each of the three quarters ending March 1943 are set forth below:

	Increase in "official" U. S. dollar assets	Sale of other Canadian U.S. dollar assets	Net increase in Canada's U. S. dollar assets
	(Millions U. S. $)		
1942			
July - Sept........	16	7	9
Oct. - Dec..........	11	7	4
Total, July - Dec. 1942.......	27	14	13
1943			
Jan. - Mar.........	51	7	44
Total, July 1942-Mar. 1943.......	78	21	57

If the present forecasts are realized, then the Canadian Government will hold liquid U. S. dollar exchange resources, as of the close of each quarter through March 1943, as follows:

End of	(Millions U. S. $)
Sept. 1942..........................	260
Dec. 1942..........................	271
March 1943..........................	322

III. CANADA'S NEEDS FOR U. S. DOLLARS

The Canadian Ministry of Finance estimates that, apart from exports made pursuant to the Hyde Park Declaration and from sales of newly-mined gold, Canada will need, July through December 1942, $393 million of U. S. dollars to cover its U. S. dollar deficit on current account and to meet maturing obligations held in this country. U. S. dollar expenditures for goods and services are placed at $762 million for the six-month period and U. S. dollar receipts on current account, exclusive of Hyde Park exports and newly-mined gold sales, at $423 million, leaving an excess of payments on current account of $339 million. Capital repayments and imports of U. S. goods lend-leased to the United Kingdom for transfer to Canada under the Hyde Park Agreement raise the estimated total for the period to $393 million.

Comparable estimates drawn up by the Canadian Government for the first quarter of 1943 show an expected U. S. dollar deficit on current account, again exclusive of Hyde Park exports and gold sales, of $152 million. Adding estimated imports of U. S. goods lend-leased to the United Kingdom for transfer to Canada and expected capital repayments to the United States to this figure brings the total of Canada's U. S. dollar needs for the first quarter of 1943 to $175 million. The anticipated small decline for this three-month period below the level of the preceding six months seems to be largely a seasonal one—receipts are expected to fall but expenditures more so.

The table below gives in summary form the Canadian Government's estimates of Canada's needs for U. S. dollars, exclusive of exports under the Hyde Park Agreement and sales of newly-mined gold, for the nine-month period, July 1942 through March 1943.

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	July-Dec. 1942	Jan.-March 1943	Total - 9 months
	(Millions U. S. $)		
A. U.S. Dollar Expenditures on Current Account			
1. Payments by Canada to U.S. for merchandise imports....................	533	249	782
2. Payments by Canada to U.S. on service account......................	211	86	297
3. Payments of U.S. dollars by Canada to non-Sterling Areas outside U.S................................	18	8	26
Total U.S. dollar expenditures...	762	343	1,105
B. U.S. Dollar Receipts on Current Account			
1. Receipts by Canada from U.S. for merchandise exports (excluding "Hyde Park" and gold exports).......	260	126	386
2. Receipts by Canada from U.S. on service account..................	112	47	159
3. Receipts of U.S. dollars by Canada from non-Sterling Areas outside U.S................................	32	11	43
4. Net receipts of U.S. dollars from Newfoundland.......................	19	7	26
Total U.S. dollar receipts.....	423	191	614
C. U.S. dollar deficit on current account exclusive of "Hyde Park" exports and newly-mined gold.....................	339	152	491
D. Bond maturities and other capital repayments to U.S......................	13	5	18
E. Imports of goods from U.S. lend-leased to U.K. and transferred to Canada, pursuant to the "Hyde Park" Agreement................................	41	18	59
Total U.S. dollar needs of Canada.	393	175	568

The various means available to the Canadian Government to satisfy Canada's needs for U. S. dollars during the next nine months are discussed below in Sections IV to VII, inclusive. The immediately following pages are devoted to a detailed examination of the summary estimates given above of Canada's U. S. dollar expenditures and receipts, first for the period July through December 1942, and then for the first quarter of 1943. As in the preceding memorandum, the estimates will be compared with previous Canadian forecasts as well as with the actual figures reported to the Treasury for past periods.

Canada's Estimated Needs for U. S. Dollars,
July through December 1942

(Millions U. S. $)

A. U. S. Dollar Expenditures on Current Account

1. Payments by Canada to U. S. for merchandise imports

a. Imports for direct war purposes.......................... 265

i. For account of Canada........................ 123

This figure is based upon estimates made by the Department of Munitions and Supply. It is exclusive of the cost of freight to the Canadian border, which is estimated by the Canadian Ministry of Finance to amount to roughly $15 million on these imports.

In addition to the above, the Canadian Government expects to receive, July through December 1942, $41 million of goods lend-leased by the United States to the United Kingdom for transfer to Canada. These imports have been included below in the tabulation of the effect of Hyde Park transactions upon Canada's U. S. dollar position. (See Section VI.)

Canadian imports of war goods from the United States for Canada's own account have risen steadily since the outbreak of war. The above estimate of $123 million for the second half of 1942 assumes a continuation of this upward trend. This figure is $28 million higher than the total of actual expenditures made by Canada on this account, January through June 1942, which in turn exceeds by $35 million the average amount spent for this purpose during each of the two previous six-month periods.

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(Millions U. S. $)

So far in 1942, however, Canadian expectations have not been fulfilled. Canadian expenditures for war imports from the United States on Canada's own account, January through June 1942, fell $21 million short of the amount forecast by the Canadian Government last March. This discrepancy is reflected in the $13 million reduction in the recent forecast received for the current six-month period.

Actual U. S. dollar expenditures of $115 million in 1941 for imports for direct war purposes, compares reasonably well with the various forecasts submitted by the Canadian Government to the Treasury during that year. Increased purchases of military vehicles accounts for most of the expected rise of $100 million, 1942 over 1941, in Canadian expenditures in the United States for imports for use in production for Canada's own account.

Estimated expenditures for the year 1942 (including cost of freight to the Canadian border) for the three principal categories of end products are: military vehicles, $87 million; machine tools and equipment, $46 million; and aircraft and parts, $35 million. The Treasury does not have a commodity breakdown of these estimates for the second half of the current year.

ii. For account of other Empire countries, principally U.K. 107

This figure is the amount forecast by the Department of Munitions and Supply reduced by roughly $20 million, the estimated cost of freight to the Canadian border. Expected expenditures on freight account are included below under services.

The above estimate of Canadian expenditures in the United States, July through December 1942, for goods to be used in Empire War Production, approximates the amount actually spent by Canada in the United States for these goods during the first six months of 1942 and is only $10-$15 million higher than the amount

(Millions U. S. $)

reported spent on this account during the last six months of 1941. Previous Canadian estimates of these expenditures, which have been submitted to the Treasury, have proved to be reasonably accurate.

The principal categories of end products covered by the estimated expenditures (including $34 million for freight) on Empire account for 1942, are as follows:

Military vehicles..................	125
Aircraft...........................	30
Machine tools and equipment........	18
Ammunition.........................	18
Other..............................	59

iii. For account of War Supplies, Ltd. 35

The three-fold expansion of this estimate over the one submitted last March for the same period reflects the sharp increase, which has occurred during recent months, in the value of U. S. Government orders placed with War Supplies, Ltd. It also represents a more realistic appraisal of the amount of U. S. components required to fill these orders.

Actual expenditures, January through June 1942, were twice as high as the Canadian Government estimated in March they would be, or $19 million as against the then estimated $9 million. The current forecast for July through December 1942, allows for roughly the same increase in absolute terms as occurred, January through June 1942 over the previous six-month period.

This item is included here for the sake of accuracy and completeness. It represents a drain on Canada's U. S. dollar resources in the short period, which drain, as in the case of the current half year, may not be offset during the same interval of time by receipts from exports incorporating the equivalent value of U. S. components. The lag between expenditures for these components and receipts from exports in the production of which they have been used, together with

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(Millions U. S. $)

the fluctuations in the amount of Canadian production on U. S. account, make this procedure of handling these expenditures the preferable one. The alternative is to subtract the value of U. S. components used from the value of Hyde Park exports, and to set the resulting figure of the net effect of Hyde Park transactions on Canada's U. S. dollar position against Canada's need for U. S. dollars, exclusive of expenditures made on behalf of War Supplies, Ltd.

b. Imports for other than direct war purposes............ 268

The current six-month period is expected to show the first substantial decrease in Canadian imports of U. S. goods for civilian use since the outbreak of the war. The above forecast is based on an expected reduction of about 8 percent, or roughly $20 million, below the actual expenditures on this account during both January through June 1942, and July through December 1941.

The estimates for this item may include expenditures for some goods which are used indirectly for war purposes, such as requirements of railroads and other essential undertakings serving the war industries or the armed forces. It may also include some U. S. components which cannot be identified with a particular piece of war equipment and which, therefore, cannot be included in the estimate of imports for direct war purposes.

Higher prices in the United States, coupled with the limitation of the Canadian Government's import subsidy program to essential civilian goods, will have a restrictive effect upon Canadian imports of non-essential goods from the United States. An increase in the per unit price of those U. S. goods which are purchased and a further expansion of Canada's war production, insofar as it entails an increase in Canadian purchases of U. S. goods for indirect war purposes, will operate to raise Canada's U. S. dollar expenditures for merchandise imports on other than direct war account.

(Millions U. S. $)

Total payments by Canada to U. S. for merchandise imports........................ 533

This represents an anticipated rise of $20 million, as compared to the first six months of 1942, and of roughly $80 million, as compared to the last six months of 1941. In each case, the rise is more than accounted for by the expected increase in imports for use in the war production. For the first time since the outbreak of war, imports of war goods, July through December 1942, are expected to equal in value imports for other than direct war uses.

The aggregate of Canadian expenditures in the United States on merchandise account, January 1, 1941 through March 31, 1942, as reported in the Canadian document submitted to the Treasury on July 27, is $100 million lower than the value of imports from the United States as shown in the Canadian official trade figures. The difference represents an adjustment of the latter figures to exclude imports not paid for by Canada as well as to correct for the artificial over-valuation of the basic customs data.

2. Payments by Canada to U. S. on service account

a. Transfers of interest, dividends and profits.... 104

This is the same as the amount reported by the Canadian Government for July through December 1941. It includes $44 million for interest payments and $60 million for transfers of dividends and profits.

The total of interest and dividend payments made by Canada to the United States has not changed substantially since the outbreak of war. Actual payments, January 1941 through June 1942 total 395 million; this is at an annual rate $20 to $30 million lower than that estimated by the Canadian Government for the years immediately preceding the outbreak of war.

b. Tourist and travel expenditures................. 7

This has been the level of Canadian tourist expenditures in the United States

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(Millions U. S. $)

during the past year. It represents a decrease of 60 percent on the basis of 1940 figures and of 80 percent, as compared to 1939.

The sharp drop in Canadian tourist expenditures in the United States since the first year of the war indicates the severity of the restrictions imposed by the Dominion Government upon Canadian travel abroad. U. S. dollar expenditures for travel are permitted only for essential health, business or educational purposes. The Canadian Minister of Finance in his budget speech of June 23, 1942, estimated that these travel restrictions had saved Canada well over $100 million of U. S. dollar exchange since they were imposed almost two years ago. He stated that no relaxations were contemplated by the Dominion Government during the foreseeable future.

c. Expenditures for freight services.............. 70

This figure is almost half again as high as the estimate submitted last March. It assumes a rise of one-fourth, or $15 million, over the amount actually spent in the United States on shipping charges, January through June 1942. This forecast increase reflects presumably both the rise in U. S. freight rates which was authorized last spring and the Canadian-anticipated change in the composition of merchandise imports from the United States; Canadian expenditures for imports from U. S. are expected to increase, July through December over January through June 1942, by only $5 million more than are Canadian payments to U. S. for freight and shipping services.

If the current forecast of $125 million for the year 1942 is realized, then Canada's expenditures in the United States for freight services in 1942 will be over twice as high as they were in 1939 and three-fifths again as high as in 1940.

Regraded Unclassified

(Millions U. S. $)

Freight paid by Canada on U. S. components used in the production of Hyde Park exports is included in the above figures. The current estimate for freight expenditures on these goods during the year 1942 is $13 million.

d. Expenditures for other services and miscellaneous income on current account............. 30

This figure covers payments for business and professional services, rents, royalties, current expenditures of Canadian diplomatic representatives, and family and church remittances.

This is the rate at which these expenditures have been running since the turn of the year. It represents an increase of one-third above the level reported by the Canadian Government for 1941.

Total payments by Canada to U. S. on service account.............................. 211

The expected increase in interest and dividend transfers and in shipping costs account for the current forecast rise of $23 million in these expenditures over the amount reported for the first six months of 1942. If this forecast proves to be accurate, Canadian expenditures on these items will total $399 million in 1942, or $50 million more than in 1941. This rise reflects anticipated increase in expenditures on freight and miscellaneous items.

3. Payments by Canada of U. S. dollars to non-Sterling Areas outside U. S.................................. 18

These expenditures are almost entirely for merchandise imports. They have been falling steadily since the outbreak of the war and during the remainder of 1942 are expected to be at a level roughly only one-half as high as a year earlier and only two-thirds as high as during the first six months of 1942.

Regraded Unclassified

(Millions U. S. $)

Of the $79 million of U. S. dollar ex-penditures reported made by Canada outside the United States in 1941, all but $5 million was on merchandise account. The remaining $5 million represented chiefly Chinese remittances.

Total estimated U. S. dollar expenditures by Canada, on current account, July through December 1942..................................	762

This estimate is about $110 million higher than the aggregate of Canada's U. S. dollar ex-penditures for goods and services during the last six months of 1941 and is $35 million more than the amount reported for the period, January through June 1942.

In each case, the rise approximates the anticipated increase in expenditures for mer-chandise imports from the United States for use in war production.

B. U. S. Dollar Receipts on Current Account

1. Receipts by Canada from U. S. for merchandise exports..	260

This figure does not cover exports of either newly-mined gold or of war goods and strategic materials made pursuant to the Hyde Park Agree-ment. In other words, it does not include either receipts from U. S. Government contracts with War Supplies, Ltd., or receipts from special metals deals with Metals Reserve and Defense Plant Cor-poration. The most important of the latter cover aluminum and lead, although small amounts of zinc concentrates, mercury, manganese, cobalt, copper and nickel are also being exported to the United States under special arrangements with these two R.F.C. subsidiaries. All other exports of base metals to the United States are covered by the above estimate, including all but a negligible proportion of nickel; (See Section VI. for a further discussion of transactions under the Hyde Park Declaration.)

The above estimate of $260 million assumes a decline of about $20 million from the level of the past year, when receipts from merchandise exports to the United States totalled around

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(Millions U. S. $)

$280 million semi-annually. The forecast decline of $20 million may reflect not so much an expected fall in total shipments as an anticipated lengthening, over the course of the year, of the lag between the receipt of merchandise in the United States and the transfer of payment by U. S. importers to Canadian exporters. The Canadian Ministry of Finance is of the opinion that payments were accelerated during the first half of the current year as a result of the widespread expectation of a change in the U.S.-Canadian exchange rate and that this acceleration in payment was one factor accounting for the excess of receipts, January through June 1942 over the March forecast. On the other hand, exports of newsprints during the remainder of this year are expected to fall below actual shipments made during January through June 1942, when inventories were being built up in this country. The current forecast drop for the second half of 1942 shows the first non-seasonal decline in Canadian merchandise exports to the United States since the outbreak of war.

If the forecast for the remainder of the year is approximated, then Canadian receipts from merchandise exports to the United States during the year 1942 (exclusive of Hyde Park exports) will exceed 1941 receipts by $33 million.

The Canadian Government reports receipts from merchandise exports to the United States (other than on Hyde Park account) of $506 million and $140 million, for the year 1941 and for the first quarter of 1942, respectively. These amounts fall a total of $50 million short of the figure given in official Canadian trade returns. Almost half of this discrepancy is accounted for by Hyde Park exports and most of the remainder is believed to represent shipments of wheat to third countries made through U. S. ports.

2. Receipts by Canada from U. S. on service account

a. Receipts for interest, dividends and profits.... 26

This figure is $7 million higher than the estimate submitted last March. It assumes a rise of $3 million in receipts for the year 1942 over 1941, as against a decline of $6 million forecast in March. Receipts from

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Canadian investments in the United States during the first half of the year totalled $24 million, or $2 million more than the Canadian Government expected last March.

The higher-than-anticipated receipts on this account so far this year are laid by the Canadian Government in considerable part to the unexpectedly large transfers made by several companies last March.

The figure of $47 million, given by the Canadian Government for 1941, is roughly $20 million higher than the various forecasts submitted during the past year. It is not strictly comparable to them, however, as it includes transfers of profits by insurance companies and other Canadian concerns in the United States which in the previous estimates were included under "miscellaneous income." (See item 2-d below, pp. 23-24.)

Canada's interest and dividend receipts from the United States in both 1939 and 1940 are estimated by the Dominion Government to have been about $27 million, roughly the amount it had forecast at various times during 1941 for that year.

b. Receipts for tourist services.................. 24

This is the same estimate submitted by the Canadian Government last March. Actual receipts, January through June 1942, totalled $18 million, or $2 million more than the Canadian Government expected in March they would be, bringing the current anticipated total for the year 1942 to $42 million.

If the above forecast for the remainder of this year is as accurate as the March estimate for the first six months proved to be, then Canada's U. S. dollar receipts in 1942, from the American tourist and other travel in Canada, will be only three-fifths as high as in 1941 and less than one-half of what they totalled in 1940. Even this low level may not be reached if nation-wide gasoline rationing is instituted in the United States, or if other limitations on

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automobile or railroad travel are imposed in both countries, with no special dispensations granted to foreigners.

The above figures for 1941 and 1942, of $70 million and $43 million, respectively, do not include American tourist expenditures which are financed by the export of American-owned capital from Canada, through the "unofficial" market for Canadian dollars in the United States. The Canadian Government, in the earlier documents submitted to the Treasury, estimated American tourist travel financed through the free exchange market at $23 million for 1941.

c. Receipts from freight and shipping............. 32

This is the amount reported for the first half of 1942 and practically the same amount that was forecast last March for the latter half of this year. The estimate assumes a rise of $10 million, or of almost 20 percent, for the year 1942 over reported receipts for 1941. This is consistent with the trend of the first two and one-half years of war.

A considerable part of the figures for this item represents payments received for freight on goods shipped through, but not to or from, Canada. Presumably the Canadian Government, in drawing up the above estimate, followed the same procedure as last March and made allowance for the particular nature of "Hyde Park" exports.

d. Receipts from other services and miscellaneous income on current account....................... 30

This is $3 million more than the income received from these sources during the first six months of 1942. It is also one-third again as large as the estimate for the last six months of 1942, submitted to the Treasury last March. The current estimate for the year is $17 million greater than the figure of $40 million reported for 1941 and estimated last March for the year 1942. Some part of this upward revision may be due to the inclusion of net expenditures by the U. S. Government in northern Canada; this item appears for the first time in this forecast.

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In addition to net expenditures of the U. S. Government in northern Canada, the figure given here covers business and professional services, rents, royalties, current expenditures of foreign diplomatic representatives, and family and church remittances. Unlike the various estimates submitted in 1941, they do not include profit transfers which have been added to interest and dividend receipts, item 2-a, p. 21 above.

Total receipts by Canada from U. S. on service account.......................... 112

If the above forecasts for various service items are reasonably correct, then Canada's receipts of U. S. dollars on service account during 1942 will be equal to what they were in 1941. So far this year, receipts for each category of services have exceeded the Canadian Government's expectations last March; the component estimates for the remainder of the year have accordingly been revised upward to reflect this favorable outlook.

3. Receipts of U. S. dollars by Canada from non-Sterling Areas outside U. S........................ 32

This estimate is $7 million lower than the amount reported for the first six months of 1942. It assumes that total U. S. dollar receipts, from non-Sterling Area countries other than the United States, during the year 1942 will fall $17 million short of the amount received in 1941. So far this year the decline has not been so sharp as forecast last March. The estimate for the remainder of the year was accordingly revised upward by $5 million to make allowance for this fact.

The decline in these receipts during the past year and a half or so has been almost entirely on merchandise account. Canadian exports to non-Sterling Area countries other than the United States paid for in U. S. dollar exchange have fallen sharply.

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Of the $88 million of U. S. dollar receipts from non-Sterling Area countries outside the United States reported for 1941, $27 million represent dividend and profit transfers. The estimate for 1942 submitted in March, which is $13 million lower than the current forecast, includes $25 million for dividends and profits.

4. Net receipts of U. S. dollars from Newfoundland...... 19

Newfoundland's net receipts of U. S. dollars have so far in 1942 been running over twice as high as last year. This relatively favorable situation may be expected to continue at least until the completion of the U. S. defense construction program there and perhaps until the close of hostilities.

The above estimate for July to December 1942, is $2 million higher than the total of net receipts turned over to Canada, January through June of this year, which in turn exceeded by $2 million the receipts for the entire year of 1941.

Total estimated U. S. dollar receipts by Canada on current account, exclusive of newly-mined gold and "Hyde Park" exports, July through December 1942........... 423

This is $13 million less than the total of U. S. dollars received by Canada, on account of these current transactions, during the first six months of this year. The drop is more than accounted for by the anticipated decline in receipts from merchandise exports to the United States.

If the above estimate for July through December 1942 is accurate, then Canada's receipts of U. S. dollars from current transactions, outside of Hyde Park Agreement and exclusive of newly-mined gold sales, will be $36 million higher during the current year than they were in 1941.

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C. Canada's estimated U. S. dollar deficit on current account, exclusive of newly-mined gold and "Hyde Park" exports, July through December 1942. . . 339

This represents an anticipated increase in Canada's U. S. dollar deficit on current account (exclusive of "Hyde Park" exports and newly-mined gold sales) of about $50 million over the amount incurred January through June 1942. It assumes a deficit for the year of $630 million, or $180 million more than the one experienced in 1941. Increased merchandise imports for use in war production are the single dominant factor.

D. Bond maturities and other capital repayments.. 13

These outpayments are discussed below in Section V., pp. 36-41. They logically belong in a tabulation of Canada's needs for U. S. dollars. Canada has to provide the dollars to meet these maturing obligations, and in the absence of capital imports she must provide them out of receipts either from current transactions or from the sale of assets.

E. Imports of U. S. goods lend-leased to the United Kingdom and transferred to Canada under the Hyde Park Agreement....................... 41

This item is included here for the sake of completeness. Presumably in the absence of the Hyde Park Agreement, Canada would need U. S. dollars to purchase these goods. A detailed discussion and tabulation of the effects of the Hyde Park Agreement are given below in Section VI., pp. 42-51.

Total U. S. dollar needs of Canada, July through December 1942.......................... 393

This is the estimated amount by which, July through December 1942, Canada's receipts of U. S. dollars on current account (exclusive of Hyde Park exports and sales of newly-mined gold) will fall short of the sum of (1) the value of goods and services received from the United States or paid for in U. S. dollars, and (2) the amount of capital repayments made to the United States.

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The above figure of $393 million allows for an increase of $69 million for the period, July through December 1942, over the amount reported for the first six months of 1942 and for a rise of $240 million for the year 1942 over 1941. The latter increment represents almost entirely an increase in expenditures for war goods.

Canada's Estimated Needs for U. S. Dollars, January through March 1943

A. U. S. Dollar Expenditures on Current Account

1. Payments by Canada to U. S. for merchandise imports.

a. Imports for direct war purposes........................ 130

i. For account of Canada............................. 57

This figure, although almost 10 percent lower than the level forecast for the current six-month period, represents an expected rise of 20 percent, or $10 million over the amount reported for the same period one year earlier. It is twice as high as expenditures made on this account during the first half of 1941.

ii. For account of other Empire countries, principally U. K.............................. 52

This is the same amount forecast for the last quarter of 1942. It assumes no increase in expenditures over the preceding year.

iii. For account of War Supplies, Ltd............ 21

This is the same estimate as for the last three months of 1942. It is two and one-half times as large as the figure reported for January through March of this year.

b. Imports for other than direct war purposes...... 119

This assumes a continuation of the decline in these expenditures which is expected by the Canadian Government to set in during the present summer.

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(Millions U. S. $)

Total payments by Canada to U. S. for merchandise imports........................ 249

This is almost $20 million lower than the three-month average of Canadian expenditures for U. S. goods during the last half of 1942. It represents a rise, however, of about $45 million over each of the first two quarters of 1941.

2. Payments by Canada to U. S. on service account

a. Transfers of interest, dividends and profits.... 42

This is $3 million higher than the total of transfers reported for the same quarter of 1942. The figure has been raised, presumably, to allow for the large purchases by Americans during recent months of multiple-payment Canadian securities. (See Section V., pp. 37-38, for a discussion of these purchases.)

b. Tourists and travel expenditures................ 4

This figure assumes no change from the level of the past year and a half.

c. Expenditures for freight services............... 25

The $4 million increase in this figure over the amount reported for the first quarter of 1942 reflects an anticipated higher per unit cost for freight services. The anticipated increase in these expenditures over the same period a year earlier is one-half as large as the expected rise in Canadian expenditures for merchandise imports from the United States.

d. Expenditures for other services and miscellaneous income on current account...................... 15

This is the level at which these expenditures have been running so far this year. It is the amount forecast for each of the last two quarters of 1942.

Total payments by Canada to U. S. on service account.............................. 86

This represents an estimated rise of $8 million over the same quarter of 1942. It reflects the anticipated increase in interest and dividend transfers and in freight expenditures.

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(Millions U. S. $)

3. Payments by Canada of U. S. dollars to non-Sterling Areas outside U. S.................................. 8

This is the same amount forecast for the last quarter of 1942. It allows for a 40 percent reduction from the same period a year earlier.

Total estimated U. S. dollar expenditures by Canada, on current account, January through March 1943.................................. 343

This figure represents the anticipated increase of only $10 million over the amount reported for the first quarter of 1942. It is more than accounted for by the expected increase in imports for account of War Supplies, Ltd.

B. U. S. Dollar Receipts on Current Account

1. Receipts by Canada from U. S. for merchandise exports.................................. 126

This assumes that the decline, in Canadian exports to the United States made outside the Hyde Park Agreement, which set in during the early part of 1942 will continue into 1943. The above forecast allows for a reduction of $14 million from the amount reported for each of the first two quarters of 1942.

2. Receipts by Canada from U. S. on service account

a. Receipts for interest, dividends and profits.... 9

This is only three-fourths as much as was actually received on this account during the first quarter of 1942. The receipts, January through March of this year, however, were unexpectedly large and exceeded the Canadian Government's expectations by $2 million.

b. Receipts for tourists services.................. 6

This allows for a slight drop from the 1942 level. The decline may be greater, however, if stringent restrictions on travel are imposed in either United States or Canada.

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(Millions U. S. $)

c. Receipts from freight and shipping.................... 16

This assumes a continuation of the level of freight receipts reported for the first half of 1942. It is the same amount as is either reported or forecast by the Canadian Government, as the case may be, for each quarter of the current year.

d. Receipts from other services and miscellaneous income on current account....................... 16

This allows for a slight rise over the last quarter of 1942. If the forecast is realized, receipts on these items will have risen by 25 percent over the course of the year.

Total receipts by Canada from U. S. on service account.......................... 47

Forecast changes in the component items about offset each other; this total figure approximates the amount of U. S. dollars reported spent on services, January through March 1942.

3. Receipts of U. S. dollars by Canada from non-Sterling Areas outside U. S.................................. 11

This assumes a sharp drop in these receipts, due presumably to an expected falling off of merchandise exports to countries other than the United States paid for in U. S. dollars. It indicates a drop of $7 million from the amount reported for the first quarter of 1942 and of $8 million compared to the forecast for the last quarter of this year.

4. Net receipts of U. S. dollars from Newfoundland...... 7

This is the same figure as was reported for the first quarter of 1942. It assumes a continuation of the present favorable situation.

Total estimated U. S. dollar receipts by Canada on current account, exclusive of newly-mined gold and "Hyde Park" exports, January through March 1943...................... 191

If the current forecast for a decline in exports to the United States outside the Hyde Park transactions is realized, then the above estimate may prove to be reasonably accurate. There seems to be

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no basis for this pessimistic prediction, concerning Canada's U. S. dollar receipts from these merchandise transactions, however, unless it is expected that some part of the exchange to be derived from exports made pursuant to the Hyde Park Declaration will be gained at the expense of sales falling outside the framework of this understanding.

C. Canada's estimated U. S. dollar deficit on current account, exclusive of newly-mined gold and "Hyde Park" exports, January through March 1943.. 152

An anticipated increase in expenditures for war goods coupled with an expected decrease in receipts from exports outside the Hyde Park Agreement more than account for the above forecast increase of $30 million over the reported deficit on account of these items for the first quarter of 1943.

D. Bond maturities and other capital repayments.. 5

This is the same as the amount reported for the first quarter of 1942 and the current forecast for the last quarter of the year. See below Section V. for further discussion of private capital transfers between Canada and the United States.

E. Imports of goods lend-leased to the United Kingdom and transferred to Canada under the Hyde Park Agreement.. 18

This is roughly the amount forecast for the last quarter of 1942. It is three times the amount reported received during the first three months of 1941.

Total U. S. dollar needs of Canada, January through March 1943.. 175

The anticipated larger deficit on merchandise account is responsible for the $44 million increase in this figure over the amount reported for the same quarter a year earlier. Events may show that the forecast is unduly pessimistic.

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IV. CANADA'S PRODUCTION AND SALE OF GOLD

The Canadian Government expects Canada's output of gold to fall one-third by the close of this year and one-half by the end of March 1943. This forecast is based, not on the anticipated effects of the recent Order-in-Council freezing gold production of each mine at the average tonnage for the first four months of 1942, but rather on the anticipated pinch of the growing labor and materials shortage. Gold mining is classified by the Canadian man-power mobilization board as an unessential industry and, for this reason, is expected to experience increasingly greater difficulties, if not almost complete failure, in recruiting new labor to fill its thinning ranks. In one province, at least, the industry was recently forbidden to take on new men so long as the serious labor shortage in base metals and other strategic minerals continues. Difficulties of securing adequate supplies are also reported to be hampering operations in Canadian gold mining fields. Restrictions upon the use of labor and materials, rather than direct limitations upon production, are the means being relied upon by the Canadian Government to reduce Canada's production of gold and to divert the resources used by this industry to more essential purposes.

According to a weekly tabulation received from the Federal Reserve Bank of New York, Canada sold $833 million of gold to the United States, September 1939 through June 1942. On the basis of information received from the Canadian Ministry of Finance, this gold was derived from three sources, as follows:

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	Sept. 1939 through Dec. 1940	January through Dec. 1941	January through June 1942	Total through June 1942
	(Millions U.S. $)			
Gold transferred from U.K. to Canada.........	227	—	—	227
Gold out of official Canadian reserves......	69	—	11	80
Newly-mined gold.........	248	185	93	526
Total sales of gold by Canada to U.S........	544	185	104	833

The figures of sales of newly-mined gold during the two periods, September 1939 through December 1940, and January through June 1942, are derivatives. The figure given for the latter period is $7 million higher than that reported by the Canadian Government. The discrepancy may be due to a difference in the time lag with which the sales are reflected in the books of the two reporting agencies. However, the Canadian-reported figure for 1941, which is used above, is also lower than the amount reported to us by the Federal Reserve Bank of New York; for this latter year, the discrepancy is $9 million.

Canada's production of gold and sales to the United States out of current output, since September 1939, are given in the table below. The figures of sales of newly-mined gold since 1940 are as reported to the Treasury by the Canadian Government.

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	Canada's Production of Gold	Canada's Sales of newly-mined gold to U. S.
	(Millions U. S. $)	
1939		
September	15	
4th quarter	45	
1940		
1st quarter	44	
2nd quarter	46	
3rd quarter	48	
4th quarter	48	
Total through 1940	246	248
1941		
1st quarter	45	49
2nd quarter	47	45
3rd quarter	48	46
4th quarter	46	45
Total for 1941	186	185
1942		
1st quarter	43	44
2nd quarter	44	42
Total, January - June 1942	87	86
Grand total, September 1939 through June 1942	519	519

The above figure, for sales of newly-mined gold to the United States since September 1939, is $7 million lower than that shown in the tabulation on the preceding page, for the reasons indicated there.

Gold production in Canada ceased expanding in September 1940. Each month since then, the total value of output has fallen short of the level of the corresponding period a year earlier. The decline, heretofore, has been negligible, but it is expected to assume significant proportions by the first part of 1943, as indicated by the Canadian Government's forecast set forth below:

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Estimated Sales of Newly-Mined Gold by Canada to the United States, July 1942 through March 1943

(Millions U. S. $)

1942	
July - Sept.	35
Oct. - Dec.	27
Total, July - December 1942	62
1943	
Jan. - March	20
Total, July 1942 - March 1943	82

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V. MOVEMENT OF PRIVATE CAPITAL BETWEEN CANADA AND THE U. S.

Between September 15, 1939, and June 30, 1942, the Canadian Government received over $300 million of U. S. dollar exchange from the sale by Canadians to Americans of securities and other assets. Debt repayments and bond maturities offset this gross inflow by one-fourth to one-third, thereby reducing Canada's net receipts of U. S. dollars, on private capital account, since the beginning of the war, to about $220 million. Private capital transfers ~~from~~ BETWEEN Canada and the United States since September 1939 are set forth in summary form below:

Capital Transactions Between the United States and Canada on Private Account, September 1939 through June 1942

	Sept. 1939-Dec. 1940	1941	Jan. thru June 1942	Total
	(Millions U. S. $)			
Capital Imports				
Sale of Canadian securities and other Canadian assets....................	27	54	77	158
Sale of U.S. securities and other U.S. assets held in Canada............	81	40	27	148
Total imports of capital................	108	94	104	306
Capital Exports				
Bond maturities............		26	10	
Other debt repayments......	—	7	2	—
Total capital exports....	41*	33	12	86*
Net inflow of capital from U.S. on private account.....	67*	61	92	220*

* The figure of capital exports from Canada to the United States, September 1939 through December 1940, is only a rough estimate; it was derived by raising by one-fourth the estimate for 1941 which was submitted the Canadian Government to the Treasury in November of that year.

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The unexpectedly large inflow of capital from the United States during the first six months of 1942 was a dominant factor in the $124 million discrepancy between the Canadian forecast and the actual change in Canada's U. S. dollar position during this period. The net flow of capital from the United States to Canada, January through June 1942, was three times as large as the Canadian Government forecast last March it would be. The significant feature of these transactions was the preponderance of Canadian bonds with a foreign payment feature.

The Canadian Ministry of Finance has raised its forecast for the nine months, July 1942 through March 1943, but the revision does not allow for an increase, in U. S. capital imports through private channels, of the proportions experienced during the first six months of this year. The new estimate indicates a drop of one-half from the level reported for January through June 1942, and the Canadian Government warns that even this low figure may not be realized. The Canadian Ministry of Finance in the document submitted to the Treasury on July 27, 1942, points out that this inflow of U. S. capital may cease during the period under review and intimates that if it does not fall substantially in the near future, the Dominion Government will take appropriate steps to see that it does.

The gross inflow of private capital from the United States to Canada is currently estimated at $59 million for the six months, July through December 1942, and gross capital outpayments from Canada to the United States, effected through official exchange channels and exclusive of reductions in the amount of U. S. dollar balances held by the Dominion Government, at $13 million for the same period. The estimates for the last quarter of the year are carried forward through March 1943; they indicate a net capital import from the United States on private account of $27 million for the first quarter of next year. This is the difference between the estimated gross inflow of $32 million and the forecast gross outflow of $5 million.

These figures do not cover capital movements on government account or capital movements effected through the unofficial exchange market. More specifically, they do not include either advance payments by U. S. Government agencies on contracts placed in Canada pursuant to the Hyde Park Agreement, or changes in the amount of U. S. dollar balances held by the Canadian Government, or reductions in American holdings of Canadian funds effected through the sale of Canadian dollars in the free exchange market. The figure of capital outpayments, however, does include a number of anticipated municipal and provincial bond redemptions.

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Estimated Transfer of Capital Between Canada and the United States, on Private Account, July through December 1942

(Millions U. S. $)

A. Flow of capital from U. S. to Canada

1. Canadian sales of U. S. securities and other U. S. assets held in Canada....................... 14

This estimate is $2 million lower than the one submitted to the Treasury last March, despite the fact that the companion estimate for the first six months of the year was $8 million or 30 percent, short of actual receipts during that period.

The downward revision of the estimate for this item seems unduly pessimistic in view of the unexpectedly large sales, January through June 1942.

2. Canadian sales of Canadian securities and other Canadian assets.................................. 45

This estimate, although twice as high as the one submitted last March, assumes a 40 percent reduction from the level reported for the period, January through June 1942. If the Canadian Government, as it contemplates doing, places an embargo on the export of Canadian securities with a foreign payment feature, this source of exchange will dry up. Of the $77 million of Canadian securities bought by Americans, January through June 1942, $67 million were Canadian bonds, all but $2 million of which provided for payment in a foreign currency. It is the large volume of sales of these foreign-payment-feature bonds, carrying with it as it does a concomitant increase in the future demand on Canada's supplies of U. S. dollar exchange to cover interest payments, which has given Canadian Government officials cause for concern.

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(Millions U. S. $)

Gross inflow of capital from U. S. on private account, July through December 1942............ 59

This represents an expected decrease of $45 million from the amount of U. S. dollar exchange derived by Canada from this source during the first half of 1942.

B. Outpayments of capital to U. S. by Canada

1. Canadian redemption of bonds held in U. S....... 11

So far this year, the amount of U. S. dollar exchange required for capital repayments has been less than the Canadian Government expected last March it would be. They have accordingly reduced their forecast for the current six-month period. This reduction represents in part a correction for the apparent overestimation of holdings of these obligations by non-residents of Canada and in part an adjustment for the successful completion of arrangements for refunding some provincial and municipal bond maturities. These refunding operations have been made possible by the suspension of Section 7a of the Neutrality Act of 1939.

Actual redemptions, January through June 1942, were $10 million instead of $13 million as forecast in March, while redemptions for the remainder of the year are now placed at $11 million instead of $26 million, the estimate submitted in the March document.

2. Other debt repayments by Canada to U. S......... 2

These repayments have been running considerably below the 1941 level. The Canadian Government has lowered its estimate for the current six-month period to allow for this fact.

Unlike the early Canadian forecasts submitted to the Treasury, the above figure does not include the withdrawal of funds from Canada by U. S. residents through the unofficial exchange market in this country. In earlier memoranda, the Canadian Government estimated

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its loss of U. S. dollar exchange, through the transfer of Canadian dollar balances by American holders to American tourists going to Canada, at $23 million per year. ____

Total capital outpayments to U. S. by Canada on private account, July through December 1942.................................. 13

If the above forecast is accurate then the total of Canada's U. S. dollar expenditures for debt repayments will be $8 million lower in 1942 than they were in 1941, instead of $12 million higher as predicted by the Canadian Government last March.

Estimated net U. S. dollar receipts by Canada on private capital account, July through December 1942............ 46

This assumes that Canada's net U. S. dollar receipts on account of private capital imports from the United States, July through December 1942, will be only half as large as they were during the first six months of this year. If the Canadian Government in the near future prohibits the export of Canadian securities to the United States, the actual inflow during the current six-month period may fall short of the above estimate; if, however, the Canadian Government does nothing to interfere with these sales and if present trends continue, the above forecast may considerably understate the amount of U. S. dollar exchange Canada will derive from this source during the remainder of this year.

Estimated Transfer of Capital Between Canada and the United States, on Private Account, January through March 1943

The estimates, submitted by the Canadian Government for the first quarter of 1943 and set forth in the tabulation below, are the same as those drawn up for the last quarter of this year. They are, therefore, subject to the same comments and qualifications made in the preceding pages concerning the latter.

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(Millions U. S. $)

A. Flow of capital from U. S. to Canada	
1. Canadian sales of U. S. securities and other U. S. assets held in Canada....................	7
2. Canadian sales of Canadian securities and other Canadian assets..................................	25
Gross inflow of capital from U. S. on private account, January through March 1943............	32
B. Outpayments of capital to U. S. by Canada	
1. Canadian redemption of bonds held in U. S.......	4
2. Other debt repayments by Canada to U. S.........	1
Total capital outpayments to U. S. by Canada on private account, January through March 1943................................	5
Estimated net U. S. dollar receipts by Canada on private capital account, January through March 1943.............	27

Because of the difference in coverage, the Canadian-reported figures of net capital transfers from the United States on private account, shown above on p. 36, cannot be compared with U. S. Treasury capital movements data. Exclusive of the movement in short-term banking funds, U. S. Treasury data show a net capital outflow from the United States to Canada of only $67 million, January 1941 through June 1942; net purchases by Americans from Canadians of U. S. securities are reported in our figures to have totalled $31 million, January 1941 through June 1942, and net purchases of foreign securities by Americans from Canadians are given at $36 million for the same period. The amount of U. S. dollar exchange reported by the Canadian Government as received during this period from the net transfer of private U. S. capital to Canada is $153 million. Part of the discrepancy between the two sets of figures can be laid to the wider coverage of the Canadian reports than of the U. S. Treasury capital movements data. Presumably the Canadian figures include long-term capital movements other than security purchases and sales, such as capital transfers between American and Canadian affiliated companies. For instance, they presumably include the capital assistance being given by the affiliated company in the United States to the International Nickel Company of Canada in connection with the $26 million expansion program of the productive capacity of the latter company in Canada. Such capital transfers would be reflected only indirectly in the Treasury capital movements data, and then only to the extent that they affect the reported amount of short-term Canadian funds held in this country.

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VI. THE EFFECTS OF HYDE PARK TRANSACTIONS ON CANADA'S U. S. DOLLAR POSITION

The Department of Munitions and Supply, in a document dated July 14, 1942 and submitted to the Canadian Ministry of Finance for use in compiling its current forecast of Canada's U. S. dollar position, estimates that transactions with the United States growing out of the Hyde Park Declaration will result in a gross contribution to Canada's U. S. dollar resources of about $300 million, July through December 1942, and of roundly $175 million, January through March 1943. Dollar receipts from these transactions are summarized in the table below.

	July thru Dec. 1942	Jan. thru March 1943	July 1942-March 1943
	(Millions U. S. $)		
A. Current yield of U.S. dollars from Hyde Park exports....................	238	145	383
B. Imports of U.S. goods lend-leased to U.K. and transferred to Canada under the Hyde Park Agreement..............	41	18	59
C. Petroleum products purchased by U.S. on account of U.K. for the British Commonwealth Air-Training Plan........	20	11	31
Gross contribution of Hyde Park Transactions to Canada's U.S. dollar resources............................	299	174	473

To make allowance for the U. S. dollar content of these exports, the figures for both the current yield of U. S. dollars and the gross contribution of Hyde Park transactions to Canada's U. S. dollar holdings have to be reduced by $29 million for the period, July through December 1942, and by $15 million for the first quarter of 1943. This leaves the estimated net effect of the Hyde Park Agreement upon Canada's U. S. dollar position during these two periods at $270 million and $160 million, respectively.

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The tabulation has been drawn up to show gross receipts from Hyde Park exports for the same reason that expenditures on behalf of War Supplies, Ltd., were included above under merchandise imports. That is, because of the almost certain discrepancy, in short intervals of time, between the aggregate of Canada's U. S. dollar expenditures incurred for imports for use in production on U. S. account and the value of the U. S. dollar content of goods shipped by Canada on those orders during the same period.

This procedure gives a more accurate picture of Canada's U. S. dollar needs for short periods. On the one hand, it shows how much U. S. dollar exchange Canada actually needed, or estimates to need, during any given period for merchandise imports from the United States and, on the other hand, how much U. S. dollar exchange she received, or expects to receive, for merchandise shipped during the same interval of time. For the period, July through December 1942, the Canadian Government estimates it will spend $35 million of U. S. dollars on account of War Supplies, Ltd., as against $29 million of U. S. goods used to produce Hyde Park exports expected to be shipped during this same six months.

If the Canadian forecast for the current six-month period is realized, Canada's U. S. dollar receipts from Hyde Park transactions will be at the annual rate which the framers of the Agreement hoped would be reached during the first year of operation.

A. Receipts from Hyde Park Exports

During the four and one-half months which elapsed between the drawing up of the current Canadian forecast of receipts from Hyde Park transactions and the one submitted last March, the U. S. Government increased its commitments to purchase Canadian munitions and strategic materials by about $500 million. This $500 million expansion in U. S. Government orders has not led to a substantial upward revision in the Canadian Government's estimate, of U. S. dollar receipts from Hyde Park transactions, for the current six-month period. The recent forecast, shown on p. 45 above, allows for an increase in the current yield of U. S. dollars from Hyde Park exports of only $30 million over the amount predicted by the Canadian Government last March. The forecast for the first quarter of 1943, however, has been raised substantially above the March prediction.

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The small anticipated rise in Hyde Park receipts for the current six-month period, shown by the Department of Munitions and Supply's estimate of July 14 over the one drawn up last February 26, is hard to reconcile with the much larger increase over the February 26 forecast shown in an estimated schedule of receipts on the then outstanding U. S. Government contracts with War Supplies, Ltd., drawn up by the same Department as of May 31, 1942. The May 31 forecast shows expected receipts on U. S. Government contracts with War Supplies, Ltd., exclusive of the ship contract which was then not yet signed, of $183 million, July through December 1942, and of $60 million, January through March 1943. This represents an increase of $100 million over the February 26 estimate for receipts from this account during this nine-month period. It allows for an increase in receipts, July 1942 through March 1943, two-fifths as large as the total value of the contracts signed with War Supplies, Ltd. between February 26 and May 31, 1942. The more conservative estimate submitted to the Canadian Ministry of Finance on July 14, may be the result of a more sober and thorough appraisal of the prospects during the immediate future and may represent a nearer approach to the actual results which may be expected during the nine months ending March 31, 1943 than did the earlier, more optimistic forecasts. It may, however, reflect nothing more than a change in the directives covering assignments of Canadian munitions production between Canadian needs, U.K. orders and War Supplies, Ltd. A decision to reduce the priority rating of War Supplies, Ltd., and to fill other orders first would, of course, be immediately reflected in a worsening of Canada's U. S. dollar prospects.

The actual effect of Hyde Park transactions, January through June 1942, on Canada's U.S. dollar position closely approximates the estimate submitted last March, but only because of the unanticipated receipt of $34 million of advance payments, April through June, largely in connection with the expanded aluminum program. In this connection, it is worth noting that no prepayments on capital advances are expected by the Canadian Government on Hyde Park transactions, during the nine-month period, July 1942 through March 1943. Rather exports valued at $36 million are expected to be made against capital advances and prepayments received before the close of June 1942.

The estimates of the Department of Munitions and Supply relative to Canada's receipts of U. S. dollars from Hyde Park exports during the nine months ending March 31, 1943, are given in summary form below:

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	July thru Dec. 1942	Jan. thru March 1943	July 1942-March 1943
	(Millions U. S. $)		
Total value of Hyde Park exports..........	258	161	419
Value of exports made against pre-payments................................	20	16	36
Current yield of U.S. dollars from Hyde Park exports......................	238	145	383
Value of U.S. materials used to produce these exports (including freight).........	29	15	44
Net current yield of U.S. dollars from Hyde Park exports................	209	130	339

The above forecast is drawn up on the assumption that the U. S. components required to produce these goods will be forthcoming and current production schedules in Canada maintained. The Canadian Ministry of Finance believes this may be an over-optimistic view.

The above figures include receipts from exports of only those metals which are the subject of special deals with Metals Reserve and Defense Plant Corporations. The vast bulk of Canadian nickel exports to the United States have accordingly been excluded from this tabulation, even though production of the International Nickel Company in Canada is being expanded, 32 million pounds per annum at a cost of $26 million; with the financial assistance of the affiliated company in the United States.

Aluminum and lead are the principal materials covered by these special deals with Metals Reserve Corporation, but a small amount of mercury, manganese, cobalt, copper, nickel and zinc are also being obtained under these arrangements. The purchase program for aluminum has been considerably stepped up since the February estimates were made and deliveries during recent months have been greatly in excess of what was then anticipated, but we do not know how much of an allowance the Department of Munitions and Supply made in its July 14 forecast either for the expansion ~~of~~ the aluminum program or for the placing of other U. S. Government orders for Canadian minerals. We have as yet not received from the Canadian Government a breakdown of those figures either as between contracts with War Supplies, Ltd., and the special material deals, or as between principal categories of commodities.

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At a meeting in the Office of the Secretary on July 21, a representative of the Metals Reserve Corporation presented estimates of net payments to be made by that agency on Canadian metal and ore purchase contracts, as follows:

	Approximate Value of Expected Deliveries		
	1942	1943	1944
	(Millions U. S. $)		
Aluminum..........................	45.6	90.0	108.0
(Made against prepayments).....	13.5	25.0	30.0
Lead (inc. ore & concs.).........	6.3 1/	.3	.3
Zinc (metal, ores & concs.)......	1.4	2.2	1.6
Nickel..........................	.8	1.4	1.4
All other........................	1.5	1.8	--
Total..........................	55.6	95.7	111.3
Aluminum delivered against advance payments, as above..............	13.5	25.0	30.0
Estimated current payments to be made against deliveries....	42.1	70.7	81.3

1/ Some of these contracts provide for maximum and minimum deliveries; figures represent maximum under contract.

In addition, the Metals Reserve Corporation has contracts under negotiation which will raise expected deliveries from Canada through 1944 by about $10 million--i.e. $1.4 million in 1942, $5.8 million in 1943, and $3.2 million in 1944. Pending contracts cover copper, lead and zinc concentrates, and alumina.

As for U. S. Government contracts with War Supplies, Ltd., airplanes, cargo ships, shells and guns together account for three-fourths of the total commitments made through June 1942. The table on the following page sets forth these contracts classified by principal types of munitions, according to the subcommittee responsible for their negotiation. It is taken with only slight changes from the statistical report recently compiled by the American Section of the Joint War Production Committee.

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Subcommittee responsible for item ordered	Accumulated Total of Contracts Signed to June 30, 1942 (Millions U. S. $)
Airplane	171
Merchant Shipbuilding	158
Shell	136
Guns	101
Communication and Fire Control	67
Mechanization & Mechanical Transport	41
Small Arms Ammunition	38
Chemicals and Explosives	11
Unclassified	31
Total of contracts signed	754

The proportion of Canadian munitions production going to War Supplies, Ltd., for the account of the U. S. Government, is expected to at least triple between the first quarter of 1942 and the third quarter of 1943. A compilation of the distribution of Canadian munitions production by country of purchase, which was also made by the American section of the Joint War Production Committee, is shown below. Since it is based on U. S. Government orders with War Supplies, Ltd., in effect on May 1, 1942, and since $265 million of additional contracts have been signed since that date, it almost certainly understates the relative importance of the U. S. Government orders in the Canadian production picture.

Distribution of Canadian Munition Production by Country of Purchase

	Canada (Percent)	U. K. and other Empire (Percent)	United States (Percent)
1941	38.1	60.2	1.7
1942			
Jan. - March	33.5	60.2	6.3
Jan. - Dec	37.1	51.9	11.0
1943			
Jan. - Sept	36.3	48.1	15.6
July - Sept	33.9	45.6	20.5

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B. Imports from U. S. lend-leased to U. K. and transferred to Canada under the Hyde Park Agreement

Canadian imports from the United States which are obtained by the United Kingdom under lend-lease for transfer to Canada have so far this year been running much higher than the Canadian Government estimated in March they would be. During the first six months of this year they were over twice as high as expected last March--i.e., they totalled $28 million. The current estimate of $41 million, for the period, July through December 1942, represents a 50 percent rise over the figure forecast made last March.

If the current estimate for the latter half of this year is realized, Canada will have received $69 million of U. S. goods during 1942 which did not require a U. S. dollar outlay on her part. These goods are received in accordance with the principles of the Hyde Park Agreement; they are paid for by the U. S. Government and charged to the United Kingdom under lend-lease.

The current forecast of $69 million represents one-third of the amount the Canadian Government now expects to spend during 1942 for imports to be used in Canada for Empire war production. The proportion of these expenditures which are offset by the receipt of goods charged to the United Kingdom under lend-lease has risen steadily. The proportion has increased from less than 12 percent for the first quarter of 1942 to a hoped-for 37 percent in the last quarter of this year.

It is not all together clear why this part of the Hyde Park Agreement has not been more successfully carried out. The intention announced by the framers of the Agreement at the time it was reached was to relieve Canada of making U. S. dollar expenditures to obtain goods needed in her production of war goods for the United Kingdom and other Empire countries. This was to be accomplished by the United Kingdom obtaining under lend-lease for transfer to Canada, either the identical goods to be used in production for British account, or the equivalent in value of such goods obtained and paid for by Canada. Slowness of lend-lease machinery during its first year of operation, initial reluctance of Canadian officials to go through lend-lease procedure, and the possibilities of adverse political repercussions in this country to Canada's obtaining such industrial goods as coal and oil under lend-lease for use in production for U. K. and Empire account, may all have contributed to the meager showing made to date under this part of the Agreement.

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A tabulation received from Lend-Lease indicates that the future outlook is more promising than the past record. Canex requisitions approved by that office up to the middle of July provide for the receipt by Canada of about $90 million of U. S. goods under this part of the Hyde Park Declaration. This is in addition to the $30 million of U. S. goods already transferred under this arrangement. Of the $90 million of U. S. goods still to be delivered under the Canex requisition already approved by Lend-Lease, $70 million represents the value of requisitions, commitment letters for which have been signed since the beginning of April.

C. Petroleum products purchased by U. S. on account of U. K. for the Empire Air-Training Plan

According to the Canadian Government, this petroleum is being purchased by the U. S. Government from American oil companies in Canada and charged under lend-lease to Great Britain. The estimate of $20 million for the six-month period, July through December 1942, and the forecast of $11 million for the first quarter of 1943 are preliminary and make no allowance for the crude petroleum which Canada will have to purchase in the United States to fill these orders. The procedure, under which these petroleum products are being provided to the Empire Air-Training Plan in Canada, is reported by the Canadians to have been agreed upon at the International Air Conference held in Ottawa last Spring.

D. Accomplishments under the Hyde Park Agreement to date

The Department of Munitions and Supply estimates that Canada has received through June 1942, as a result of the Hyde Park Agreement, $200 million of U. S. exchange as payment for goods produced for the account of the United States and $30 million of U. S. goods charged under lend-lease to the United Kingdom. These are gross figures which must be reduced by the estimated amount of U. S. components used in the production of Hyde Park exports in order to arrive at an estimate of the net contribution to Canada's U. S. dollar position made during this period by Hyde Park transactions. U. S. components used in these exports through June 1942 are placed at $20 million, and the net contribution of these transactions to Canada's U. S. dollar holdings during the first year of operations at, therefore, $210 million. The table on the following page summarizes the effect through June 1942 of the transactions undertaken by Canada with the United States pursuant to the Hyde Park Declaration.

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	Thru Dec. 1941	Jan. thru June 1942	Total thru June 1942
	(Millions U. S. $)		
Value of Hyde Park exports..................	8	69	77
Deduct exports made against prepayments.....	-	7	7
Add prepayments and capital advances........	50	78	128
Current yield of U. S. dollars from Hyde Park exports............................	58	140	198
Add imports of U. S. goods lend-leased to U. K. and transferred to Canada under Hyde Park................................	3	28	31
Gross contribution of Hyde Park transactions to Canada's U. S. dollar resources................................	61	168	229
Deduct U. S. dollar content of Hyde Park exports, shown above....................	3	18	21
Net effect of Hyde Park transactions on Canada's U. S. dollar position............	58	150	208

Of the $58 million received by the close of 1941 on Hyde Park exports, $50 million represents prepayments for aluminum and $7 million was received for lead delivered to the Metals Reserve Corporation. Through December 1941, Canada received less than $2 million of U. S. dollar exchange on U. S. Government orders placed with War Supplies, Ltd., and only $3 million of U. S. goods obtained by the United Kingdom under lend-lease for transfer to Canada.

Prepayments continued to be the largest source of U. S. dollar receipts on Hyde Park transactions during the first half of this year. Canada's receipts of U. S. dollars, on account of U. S. Government contracts, through June 1942, approximated the $200 to $300 million annual goal mentioned in the Declaration.

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E. The outlook after March 1943

If U. S. Government orders in Canada are not curtailed and the present program is maintained for sometime in the future, then receipts of the magnitude forecast for the nine months ending March 1943 may be expected to be continued indefinitely into the future. The slight increase shown in the latest forecast for the last six months of 1942 over the estimate submitted last March, coupled with the large aggregate of orders signed by the U. S. Government since the close of February, indicates that actual receipts, during the months immediately following the close of March 1943, may be at a higher rate than the estimate for the current nine-month period. Likewise, the outlook would seem to be for an increase in the value of U. S. goods lend-leased to the United Kingdom and transferred to Canada. This, of course, assumes that U. S. goods necessary to maintain present production schedule in Canada are forthcoming.

All in all in the absence of any unforeseen unfavorable developments, the effect of Hyde Park transactions upon Canada's U. S. dollar position may be expected to be even greater after March 1943, than during the immediately preceding months.

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VII. CANADA'S STERLING POSITION

We have attempted below to draw together a picture of Canada's financial position vis-a-vis the Sterling Area since the outbreak of war in September 1939. The data are taken almost entirely from official sources, most important of which are speeches delivered by Mr. Ilsley, Minister of Finance, on March 18 and June 23, 1942, confidential documents submitted by the Canadian Government to the Treasury at various times during 1941, and memoranda received from the British Government containing the information presented by the Treasury to Congress in January 1941.

A. The Sterling Area's cash deficiency of Canadian dollars, September 1939 through June 1942

Canada has contributed roughly the equivalent of US$ 2 billion of goods and services to the Sterling Area, September 1939 through June 1942. This is the amount by which during this period, the receipts of Canadian dollars by Sterling Area countries for goods and services exported to Canada fell short of expenditures made in Canada on their behalf. Of this $2 billion total, all but $225 million was financed by Canada; and of the $1.8 billion financed by Canada, all but $115 million represented a drain on the public Treasury.

The table on the next page shows the various means by which this $2 billion cash deficiency of the Sterling Area vis-a-vis Canada has been settled. The figures were compiled on the basis of one assumption which may not be true in fact. This assumption is that no further repatriations have been carried out under the U. K. War Financing Act, beyond the $200 million reported by Mr. Ilsley in his speech of June 23, 1942. The distribution of the figures between the different periods may also not be entirely accurate; it is in part ours made on the basis of data at hand.

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Methods of Financing the Sterling Area's Cash Deficiency of Canadian Dollars, September 1939 through June 1942

	Sept. 15, 1939-Dec. 31, 1940	Jan. thru Dec. 1941	Jan. thru June 1942	Total thru June 1942
	(Millions U. S. $)			
Transfer of gold to Canada by U. K.	227	--	--	227
Private repatriation of U.K.-held Canadian securities, and other private transfers of capital........................	45	70	--	115
Total financed by Canadian Government:				
Repatriation of Dominion securities....................	191	169	203	563
Accumulation of sterling balances or extension of gift........................	78	657	387	1,122
Total cash deficiency of Canadian dollars..................	541	896	590	2,027

As indicated by the penultimate item in the above table, Canada's financial relations with the United Kingdom and the rest of the Sterling Area have been put on a new footing in accordance with the U. K. War Financing Act passed in March 1942.

First, almost US$ 400 of the US$ 900 million gift provided for in that Act has been already used up. If the rate of expenditure reported for the first quarter of the current fiscal year continues, the gift will be exhausted before the close of 1942. The original expectation was that it would take care of the requirements of the United Kingdom for Canadian dollars until sometime early in 1943.

This forecast was based on the assumption that the Sterling Area's deficit of Canadian dollars during the last nine months of this year would be at roughly the same level as in the fiscal year 1941-42. The disbursements reported made under the U.K. War Financing Act during the quarter, April through June 1942, are at a higher-than-average level for the preceding year, even after allowing for the inclusion of US$ 69 million of past accumulations of sterling in the figure of US$ 393 million disbursements made through June. We do not know whether this increase reflects a permanent trend or whether it is merely due to a change in the mechanics of bookkeeping. It is generally expected that when the current appropriation is exhausted provision will be made to continue the free gift arrangement.

Under the arrangement, the Dominion Government provides the United Kingdom with Canadian dollars to purchase munitions, food and raw materials in Canada. It is designed to take care of Britain's needs for Canadian dollars over and above what she obtains from exports of merchandise and services to Canada.

Secondly, at least US$ 200 million of the estimated US$ 265 million of Dominion Government and Canadian National Railway securities held in the United Kingdom at the time of the passage of the U. K. War Financing Act, have already been repatriated in accordance with the provisions of that Act. Two hundred million is the amount reported by the Canadian Minister of Finance in his speech on June 23 as having been charged to the account for the fiscal year 1941-42. We have no information as to whether on June 23, $60 million of these securities remained to be repatriated and, if so, whether any or all of this $60 million bloc have since been transferred, or whether the differential between the amount reported repatriated on June 23 and the total estimated last March as held in the United Kingdom represents an error in that estimate.

Thirdly, the operation, to convert US$ 630 million of the past sterling accumulations shown in the table above into a Canadian dollar obligation of the British Government, has already been completed. Any balances remaining over and above this loan, plus the amount used in repatriating the securities, plus the amount charged to the gift, are presumably necessary to conduct the current operations of the Canadian Foreign Exchange Control Board.

The amount of the US$ 630 million loan is to be reduced during the war by the proceeds from any redemption or repayment of Canadian securities owned in Britain, as well as by the proceeds of any sales to persons outside the United Kingdom of Canadian dollar securities owned by residents of the United Kingdom. This leaves the British Government free to use the proceeds of U. K. sales outside the United Kingdom of Canadian sterling securities for purposes other than the reduction of this loan.

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In addition to the securities whose repatriation was provided for by the U. K. War Financing Act, the Canadian Minister of Finance in introducing that resolution estimated that U. K. residents hold an aggregate of US$ 630 million of Canadian dollar securities, or to an amount roughly equivalent to the face value of the Canadian dollar loan to the British Government, and about US$ 270 million of Canadian sterling securities. These figures are roughly 50 percent lower than the estimate of the Dominion Bureau of Statistics for 1937, adjusted for repatriation operations, would indicate. On the basis of this estimate of the Dominion Bureau of Statistics, British residents still have investments in Canada with an aggregate value of over US$ 1,500 million.

As pointed out by Canadian officials, the change in the financial arrangement will not alter the amount of money which the Canadian Government will have to raise. So far as concerns past accumulations, it merely converts a demand sterling liability on the British Government into a fixed Canadian dollar obligation and, so far as concerns future transactions, it merely means that the Canadian Government will no longer receive an equivalent sterling credit for funds paid out by it to finance British expenditures in Canada. The table below shows the increase in the amount of financial assistance given by Canada to the United Kingdom as well as the rise in the direct war expenditures of the Dominion Government.

The Canadian Government Expenditures on War Account
Since September 1939

	1939-1940	1940-1941	1941-1942 (prel.)	1942-1943 (est.)
	(Millions U. S. $)			
Direct war expenditures...............	110	675	1,200	2,000
Financial assistance to U.K.............	100	400	950	1,000
Total............	210	1,075	2,150	3,000
Percentage that financial assistance to U.K. is of the total.	48%	37%	44%	33%

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B. Canada's expenditures and receipts of sterling, September 1939 through December 1941

According to official Canadian statements, the Dominion Government during the period, September 1939 through December 1941, had a net surplus of sterling receipts on current account of the equivalent of US$ 1,435 million.

British figures submitted to the Treasury for presentation to Congress in January 1941 included a tabulation of sterling expenditures and receipts of Canada and Newfoundland for the first sixteen months of war. Mr. Ilsley on March 18, 1942, gave figures of Canada's sterling expenditures and receipts on merchandise account for the year 1941. On the basis of these reported figures and the Canadian Government estimates for 1941 submitted to the Treasury in July of that year, we have attempted to construct the balance of payments on current account between Canada and the Sterling Area, September 1939 through December 1941. This tabulation shows Canada's receipts of sterling during this sixteen-month period to have been the equivalent of US$ 2,330 million and Canada's sterling expenditures US$ 895 million, as follows:

	Sept. 15, 1939 thru Dec. 31, 1940	Jan. thru Dec. 1941	Total thru Dec. 1941
	(Millions U. S. $)		
Receipts of sterling by Canada:			
Merchandise exports to U.K.	775	630	1,405
Merchandise exports to other Sterling Area	125	270	395
Other receipts from the Sterling Area	10	520	530
Total sterling receipts	910	1,420	2,330
Expenditures of sterling by Canada:			
Merchandise imports from U.K.	165	120	285
Merchandise imports from other Sterling Area	100	130	230
Maintenance of Canadian armed forces abroad	20	180	200
Other expenditures, principally interest and dividends	85	95	180
Total sterling expenditures	370	525	895
Net surplus of sterling receipts by Canada	540	895	1,435

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The above figures for the first sixteen months of war are lower than those presented to Congress by the amount reported by the British for merchandise trade between Newfoundland and the United Kingdom. The figure of $520 million for "other receipts from the Sterling Area" during 1941 is a residual item and is in no way comparable to the British-reported figure for this category of expenditures during the first sixteen months of war. Some part of the rise undoubtedly reflects increased Empire expenditures in Canada in connection with the Empire air-training program, but the figure probably also includes a substantial amount for British capital assistance and prepayments to Canadian contractors; prepayments and capital assistance for the first sixteen months of war are believed to be included, in the tabulations for this period, in receipts for merchandise exports. This is indicated by the fact that the above-reported figure of Canada's receipts of sterling for merchandise exports, September 1939 through December 1940, is over $200 million higher than the value of Canadian exports to these countries given in the official Canadian trade statistics, while the above figure for the year 1941 is only $40 million higher than the amount shown in the official trade data.

We have no information on Canada's anticipated balance of accounts with the Sterling Area for the immediate future beyond the expected net Canadian dollar cash deficiency of these countries. This is currently estimated by the Canadian Government to be the equivalent of roughly US$ 1,000 million per annum.

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COPY

No. 188

THE FOREIGN SERVICE
OF THE
UNITED STATES OF AMERICA

AMERICAN CONSULATE GENERAL
Istanbul, Turkey, November 16, 1942.

SUBJECT: Transmitting Bulgarian Anti-Jewish Law of August 29, 1942, with Comments.

THE HONORABLE
THE SECRETARY OF STATE,
WASHINGTON.

SIR:

I have the honor to transmit herewith a free translation of the Law of August 29, 1942, which was published on the basis of a law authorizing the Bulgarian cabinet to take necessary measures in connection with the regulation of the Jewish question. The source of the enclosed translation is the DURZHAVEN VESTINIK (State Gazette) No. 192, published in Sofia, Bulgaria, August 29, 1942.

A commentary on the Law, in the form of an outline of its principal provisions, which has been prepared by Dr. Floyd H. Black, follows below.

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The commentary on the Law of August 29, 1942, which follows below, may be divided as follows:

1. Jewish population of Bulgaria and participation of Jews in the economic and community life of the country.

2. Development of anti-Semitism in Bulgaria.

3. Laws against the Jews.

a) The Law of January 23, 1941 having as its aim the impoverishment of the Jews.

b) The Law of August 29, 1942, having as its aim the complete destruction of the Jewish community in Bulgaria and particularly in Sofia.

4. A resume of some of the principal articles of the Law of August 29, 1942.

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The total Jewish population of Bulgaria not including the recently annexed areas is approximately 46,000. Of these between 25,000 and 30,000 live in Sofia or between seven and eight per cent of the total population of this city. In general the Jews in Bulgaria are a respected and cultured element in the population. Their average standard of living in the country. Until the rise of Hitler to power in Germany there had never been an anti Jewish movement in Bulgaria. Jews took part in all phases of business and community life. They regarded themselves as an essential part of the State. They felt no distinction between themselves and other Bulgarian citizens. Their ancestors had come to Bulgaria in Turkish times, many families being able to trace their descent in Bulgaria as far back as 200 years.

Anti-Semitism first showed itself in forms of annoyance to Jews. Social ostracis began to appear. By 1935 petty persecution had begun. The Jews were called "cherfuti" the equivalent of the English "sheeny." Two youth organizations were formed which had had their purpose, among other things, the persecution of the Jews. These organizations were called (1) the LEGIONERI and, (2) the RATNITEI. The latter word means "workers" or "pioneers." The membership of these organizations was made up mainly of students in the gymnasiums and universities and of other young people. Both organizations had patrons and promoters in high quarters. The symbol of the LEGIONERI was a circle with a cross in it. This symbol was used as an anti-Jewish symbol, the opposite of the Jewish Star of David. This sign was seen in every conspicuous place - on walls, fences, trees, on rocks by mountain paths. It was universal. It was put on with chalk, charcoal or red paint.

Jews were beaten. Jewish children going to school were attacked by other children. About 1938 (exact date not available) a concert was given in the large concert hall "Bulgaria" by a Jewish orchestra and choir. Most of the audience, though not all, was made up of Jews. As the audience left the hall it was attacked by a crowd with eggs. In the autumn of 1939 between five and six o'clock one afternoon the windows of almost every Jewish shop in Sofia were broken simultaneously. Thus, before the war began a definite movement of persecution toward the Jews had been inaugurated.

Laws Against the Jews.

There are two principal laws against the Jews. The first, called the Law for the Defense of the Nation, went into effect January 23, 1941. The second is the law now under discussion which went into effect on August 29, 1942. A copy of the first law is not available at the present time but can probably be supplied later. Some of the main points in this law are as follows:

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1. The term "Jewish descent" is defined.

2. The registration of all Jews is required.

3. A fixed tax, or capital levy, of 20 to 25% on the total valuation of Jewish property is provided.

4. Jews are forbidden to engage in certain professions and industries. For example they are not allowed to bid on State contracts. Jews can not operate cinemas or theaters or own pharmacies or drug stores or carry on any trade in drugs, medicines and sanitary equipment. The number of Jewish doctors, dentists, and lawyers allowed to practice must be only in proportion to the Jewish percentage of the total population of any town, e.g. if 5% of the population is Jewish, then 5% of the lawyers may be Jewish.

5. Jews are not allowed to use Bulgarian terminations "ev, "ov", "sky" and others on their Jewish names.

6. Jews are forbidden to marry Bulgarians. A percentage of Jews is fixed for admission into all schools.

7. Exemption from some of these restrictions are granted to Jews who were decorated for valor in the World War, war invalids, widows and orphans, and to Jews who had been converted to Christianity before a certain date.

The purpose of this law was the restriction, robbery and humiliation of the Jewish population. A large percentage of the Jewish population of Bulgaria was thrown out of employment and impoverished by this law.

<u>The Law of August 29, 1942.</u>

As already stated the purpose of the law of January 23, 1941, was the restriction, robbery and humiliation of the Jews in Bulgaria. The purpose of this second law is the complete destruction of the Jewish community in Bulgaria. An outline of the principal contents of this law follows:

<u>Organization</u>.

The Law creates a Commissariat or Department of Jewish Affairs under the Ministry of Interior. The head of this Department is called the Commissioner for Jewish Affairs. The first Commissioner appointed, and who now holds this post, is Alexander Belev, the author of the Law. The Commissioner is assisted by a Council composed of the following representatives: one member of the Supreme Administrative Court, appointed by the Minister of Justice, one member of the Ministry of Commerce, one of the Ministry of Interior,

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one of the Ministry of Labor, one of the Ministry of Finance, one of the Bulgarian National Bank and one of the Civilian Mobilization. Great power is invested in the Commissioner and there is no appeal from his decisions. The expenses of the Department of Jewish Affairs are paid by the so-called "Fund Jewish Communities." This fund is collected from several sources: first, by a general tax of 20 to 25 per cent of Jewish property in accordance with the Law of January 23, 1941; second by a tax on Jewish bank accounts beginning with 5 per cent on accounts of 100,000 leva and rising to 12 per cent on accounts of one million leva or more, the incomes from Jewish synagogues, schools and other Jewish institutions or organizations. This fund is used to pay the expenses of Jewish communities, to help poor Jews, to provide for the settlement of Jews in villages and camps, and to pay the salaries of members of the Council and of the employees of the Department of Jewish Affairs. Each Jewish community will have its own Jewish council of four to six members appointed by the Commissioner to handle its affairs including the control of Jewish schools, synagogues and other institutions and also to prepare for the deportation of Jews in accordance with Article 29 of the present law.

Definition of Term "Jewish Descent."

All persons are of Jewish descent:

1. Whose parents or grandparents are or were of the Jewish religion;

2. In case one of the parents or either two or three of the grandparents were of the Jewish religion;

3. In case one grandparent was of the Jewish religion and one other converted to the Jewish religion. Further details regarding descent may be found in Article 8 of the Law. Article 9 states "Whatever his citizenship or origin every person is considered of Jewish descent who was of the Jewish religion or had been converted to the Jewish religion before September 1, 1942."

4. Children born from the marriage of a Jew who is a Bulgarian citizen with a Bulgarian are not regarded as Jewish if the marriage took place before September 1, 1940, and was celebrated according to the Christian ritual, or if the Jewish parent had become a Christian before January 23, 1941.

Restrictions Enforced on Jews.

1. All Jews must make declaration of origin. This includes Jews who are Bulgarian citizens and Jews holding foreign citizenship.

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2. All persons of Jewish descent must have Jewish names. They are not allowed Bulgarian given names or family names or Jewish names with Bulgarian suffixes such as "ov", "ev", "ich", "sky", et cetera.

3. All Jews must wear the yellow badge - the Star of David - prominently displayed on an outer garment, such as the lapel of the coat or overcoat. These badges are made of cheap composition material and are sold to Jews at 20 leva each. The profits from the sale of these badges are supposed to go to the "Fund Jewish Communities." This regulation went into effect on September 29, 1942. The fact that the Bulgarian population took no notice of the badge indicated popular disapproval of the measure. By this date a great many people in Bulgaria had become sympathetic toward the Jews. Children under ten years of age and Jewish travellers holding tourist visas are not required to wear the badge.

4. Jews wearing badges may be refused admission to any establishment as hotels, restaurants, cafes, et cetera, by the owner of the establishment by the police or by a member of the Council for Jewish Affairs. A Jew may not live in an apartment or share an apartment with a Bulgarian unless they are relatives.

5. Jews can not stay in a hotel for more than ten days within any period of six months.

6. From September 15, 1942 all Jews must have a special sign reading "Jewish residence" or "Jewish business" prominently displayed over the door of their living or business premises.

7. Jews are not allowed to own cars, radios or have a telephone in their homes. Jews are forbidden to employ Bulgarian servants. It is apparent that a number of these regulations have as their purpose the humiliation of the Jews.

<u>Place of Residence and Deportation of Jews</u>.

1. Jewish families of two persons may have only one room; families of three or four persons are allowed two rooms; families of five or six persons are allowed three rooms; and families of more than six persons are allowed four rooms. Kitchens, halls and bathrooms are not considered as rooms. This regulation is due in part to the overcrowding of Sofia but mainly to the desire of the Germans and Bulgarians to get possession of the Jewish apartments of the better grade.

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2. Article 27 of the present law authorizes the Commissioner and Council to designate the streets and areas in any town where Jews must live, that is, to establish Jewish quarters or ghettos. A Jewish quarter was in fact established in Sofia in September of this year and all Jews living outside the district were ordered to move into it immediately. The physical impossibility of carrying out the order has lead to some easing up on its enforcement.

3. Jews can not leave the towns in which they reside without permission of the police.

4. The most oppressive article in the Law, Article 29, reads as follows: "Jews living in Sofia are subject to deportation to the provinces or outside of the country. In any case by November 1, 1942, all Jews living in Sofia who are unemployed in accordance with the Law for National Defense, or in accordance with the present decree, and who have no other occupation, must be deported."

We are reliably informed from Sofia that deportations under this article have already begun and that several thousand people are being rounded up for immediate deportation. The destination of the deportees is not known.

<u>Restrictions on Jewish Business Enterprises.</u>

1. Jews who are not allowed to engage in commerce and industry can not invest their capital in any other business enterprise. Jews are not allowed to open any new business enterprise.

2. Jews who have been allowed to retain their occupational rights are not allowed:

a. to hold more than one job.
b. to enlarge their businesses.
c. to form new business connections.
d. to invest more than 500,000 leva ($5952 at $4 leva equals one dollar) and this must be invested in one enterprise only.

3. Jews are entirely debarred from working in certain enterprises. Article 33 reads in part as follows: "Jews are debarred from production of or trade in medicines, sanitary materials, optical instruments and chemicals, and they can not own pharmacies, drug stores, clinics, et cetera." Jews are also debarred from industries, mines, trade in agricultural products, import and export, shipping transport and commission agencies. Jewish small craftsmen may continue to work if their working capital does not exceed 200,000 leva ($2380.00 at $4 leva to one dollar).

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4. Jews practicing professions henceforth closed to them must liquidate by October 29, 1942.

5. Jews debarred from commerce and industry by this act must deposit all their shares and holdings of any sort in the National Bank within two weeks after the law goes into effect. The proceeds will be turned over to the "Fund Jewish Communities." Failure to conform to this regulation will be penalized by a fine of two million leva or ten years imprisonment.

6. Jews thrown out of employment by these two laws can not take a new job without the consent of the appropriate labor organization and of the Department for Jewish Affairs. This means that most of them will not be able to obtain any employment for permission by the two bodies mentioned will not be given.

7. The working staff in Jewish enterprises working only with Jews must be entirely Jewish. No enterprise in which Jews are allowed to work in accordance with the Law for National Defense can have a personnel which is more than 25 per cent Jewish. In such enterprises Jews are not allowed to become managers, directors, legal counselors, commercial agents, technical advisors, bookkeepers and cashiers. This reduces the employment of Jews in any business to the lowest grades.

Jewish Properties and Capital.

Within one month after the publication of the Law for National Defense of January 23, 1941, all Jews had to declare to the National Bank all their movable and immovable property owned in Bulgaria. This regulation applied to Jews living abroad as well as those living in Bulgaria. It is enforced in the greatest detail. Property confiscated under this law becomes the property of the Government without any further proceeding or court procedure.

1. Jews cannot dispose of their movable property except their wages and household articles not exceeding 10,000 leva in value. If they wish to sell movable properties in excess of this amount the permission of the Commissioner for Jewish Affairs must be obtained.

2. In addition to the declaration of their movable and immovable properties Jews must deposit in the National Bank or local bank all securities, stocks and bonds and valuables of all sorts including watches, rings, earrings and precious stones. All these will be sold and the proceeds will be placed in the blocked account of the owner.

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3. Money may be drawn from blocked accounts for certain purposes approved by the Department of Jewish Affairs and for the support of the owner and his family if he has no other income; in any case not more than 6000 leva can be drawn in any one month for the support of the owner and his family.

Exceptions.

Jews who are Bulgarian citizens and who were married by a Christian ceremony before September 1, 1940, to Bulgarian citizens and who had been baptized before January 23, 1941, are exempted from the restrictions of this law.

Further Comment on this law.

Reports received from Sofia on November 13, 1942, indicate that this law is being rigorously enforced. Previous reports that there was some lenity in the enforcement of the law applied only to a small number of Christian Jews with regard to wearing the Star of David. Also some postponement was found necessary due to the physical impossibility of moving so many Jews into the ghetto or deporting them at one time. A prominent Jewish surgeon arrived in Istanbul from Sofia on November 12 after having been deprived of his right to practice his profession. He owned and operated a hospital and clinic, which is forbidden to Jews in accordance with Article 33 of the Law. All his property was taken away from him. Actually this man is a Catholic and has been such for thirty-five years. He declared that the reason for his severe treatment is the jealousy of Bulgarian surgeons and doctors who take this means of ridding themselves of competition.

As has already been mentioned several thousand Jews are now in the process of being deported from Sofia. Where they will be sent is not known. They are supposed to be deported to towns and villages in Bulgaria but some high placed persons believe many of them will be deported to Poland. Some think they will be put in concentration camps inside of Bulgaria where many will eventually die of disease and starvation. Others, including the surgeon referred to above, think that a large proportion of them will be shot, as they have been in Belgrade and other cities. In any case, the content of the law, together with the severity with which it is being enforced show that its purpose is the complete destruction of the Jewish community in Sofia.

Respectfully yours,

Samuel W. Honaker
American Consul General

Enclosure:
Law of August 29, 1942.
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FHB/sa
To Department in original
and hectograph.

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NOT TO BE RE-TRANSMITTED

COPY NO. 13

BRITISH MOST SECRET
U.S. SECRET

OPTEL No. 295

Information received up to 7 A.M., 29th August, 1942.

1. NAVAL

It is reported that shore installations on the North Coast of Nova Zembla have been bombarded by U-Boat or possibly an enemy raider.

2. MILITARY

No operations of importance have been reported from Egypt or Russia.

3. AIR OPERATIONS

WESTERN FRONT 27th/28th. Kassel. 222 aircraft dropped about 520 tons of high explosive and incendiaries including 71 bombs of 4,000 lb. and 81 of 2,000 lb. Assisted by flares, most crews identified their objective clearly. The attack was concentrated and successful. Many large fires were reported especially in the railway centre. Hits were reported on the Henschel Works and the Gasworks. Hurricane bombers attacked enemy shipping off Guernsey. Two vessels of 1,000 tons were set on fire and two others damaged.

28th. 11 United States Fortresses bombed Meaulte Airframe Factory near Albert from 24,000 feet. About 22 tons of bombs were dropped and bursts were reported on the objective. The close support wing of the fighter escort destroyed one Focke Wulf 190 probably destroyed five and damaged two for the loss of one Spitfire. 18 enemy aircraft were reported mainly over South-western districts. One Focke Wulf 190 was destroyed.

28th/29th. 294 aircraft were sent out, Nurnberg 159 (120 heavy), Saarbrucken 111, 'Intruders' 21, Leaflets 3.

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Preliminary reports. Nurnberg - excellent weather, good visibility, many fires started, raid successful. 20 bombers missing. Saarbrucken - visibility good, but heavy ground haze, fires somewhat scattered. 10 bombers missing. 14 enemy aircraft flew over and 2 were destroyed and 2 damaged.

MEDITERRANEAN 26/27. Our medium bombers set on fire a tanker or large merchant vessel off Crete.

27th. 9 Beauforts and 5 bomb-carrying Beaufighters, escorted by 5 Beaufighters, attacked a southbound 7,000 ton vessel and 2 Destroyers south of Greece, the attack is reported as successful. A southbound vessel escorted by a Destroyer was attacked off Apollonia. The ship was hit with torpedoes and bombs and set on fire. One enemy aircraft was destroyed and another damaged. One Beaufighter is missing.

SICILY 28th. 22 Spitfires from Malta escorted by 31 more Spitfires made a low level attack on the aerodrome at Comiso, Biscari and Gela. 6 enemy aircraft were shot down, 4 probably destroyed and 1 damaged. On the ground 10 aircraft were destroyed or probably destroyed and 4 damaged. Aerodromes and ground targets were machine-gunned. Two Spitfires are missing.

4. HOME SECURITY

28th. Bristol.. One bomb killed 37 persons, the majority being passengers in two busses. Some damage was also done to utility services.

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BRITISH MOST SECRET
U.S. SECRET

COPY NO. 13

OPTEL No. 296

Information received up to 7 A.M., 30th August, 1942.

1. NAVAL

HOME WATERS. 29th. Two motor launches at FOLKESTONE were damaged by 2 enemy aircraft, one of which was probably damaged.

NORTHERN WATERS. 28th. A U-boat shelled a lighthouse south of NOVA ZEMBLA.

ATTACKS ON TRADE. From 26th to 28th August, 10 ships were reported attacked by submarines, 8 between 19th and 27th August, and 2 much earlier. 1 Norwegian and 3 British ships were torpedoed in an outward bound convoy in North-Western approaches, and a Dutch ship torpedoed and a Norwegian shelled in the same area. A British tanker sunk in GULF OF ST. LAWRENCE (belated report) a British schooner and a Vichy French ship (belated report) in CARIBBEAN SEA and a British ship North West MADEIRA. A British ship previously reported mined off LOWESTOFT has been refloated. A United States ship reported overdue has arrived.

2. MILITARY

RUSSIA. The Russians continue their attacks against the German positions at points in the Northern and Central sectors. Southwards of VORONEZH, their attempts to establish a footing on the Southern bank of the DON appear to be meeting with success. In the middle DON sector, the Germans have made progress towards STALINGRAD from the west as well as from the Northwest, though Russians continue to resist strongly.

3. AIR OPERATIONS

28th/29th. Bombs dropped at NURNBURG and SAARBRUCKEN totalled 253 and 117 tons respectively.

29th. 12 escorted U.S.A. Fortresses made an accurate high-level attack on COURTRAI aerodrome. Other successful raids were wharves at OSTEND (11 Bostons); Power station at COMINES (6 Bostons) and PONT-A-VENDIN (2 Mosquitos). Fighter escorts and diversions involved 28 squadrons. Enemy casualties: 2 destroyed, 3 probably destroyed and 7 damaged. 2 Spitfires, a Boston and a Mosquito were lost. 8 hostile aircraft crossed our coast, causing slight damage at SWINDON, BRIGHTON and in CORNWALL. One Junkers 88 was destroyed off LUNDY ISLE.

MALTA. On 28th and 29th our fighters (2 missing) destroyed or probably destroyed 3 enemy raiders and damaged 3 others.

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MEDITERRANEAN. 27th. An enemy merchant vessel escorted by one destroyer and 2 aircraft was intercepted. Beaufighters attacked scoring one hit on ship's stern and leaving destroyer smoking from low level machine-gun and cannon fire attack. Beauforts then attacked with torpedoes, scoring 3 hits on ship, which blew up and was left on fire with decks awash and back broken. One escorting aircraft was shot down and another damaged by Beaufighters.

SICILY. Reference OPTEL No. 295, enemy casualties should read: 10 destroyed, 9 probably destroyed and 5 damaged in the air and on the ground.

EGYPT. 25th. Blenheims destroyed 9 aircraft on MAKTILA landing-ground. Night 27th/28th. Wellingtons sank a ship in an escorted convoy off DERNA.

On 27th and 28th our aircraft (4 missing) bombed and machine gunned enemy camps and mechanical transport in forward area. 1 enemy aircraft was probably destroyed and 2 damaged.

BURMA. 26th. MYITKYINA aerodrome was bombed by 15 Allied aircraft. On 28th, 6 Blenheims attacked MAGWE aerodrome.

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August 31, 1942
11:20 a.m.

GROUP

Present: Mr. Sullivan
Mr. Cairns
Mr. Blough
Mr. Viner
Mr. Thompson
Mr. Graves
Mr. Gamble
Mr. Kuhn
Mr. Gaston
Mr. White
Mr. Haas
Mr. Schwarz
Mrs. Klotz

H.M.JR: Well, I will knock on wood, but the effects around of that tax story were good. Particularly I like the Tribune. Will you please serve notice on the Commissioner for me that if he does not like the plan I, Henry Morgenthau, Jr., ask him to please keep quiet until he sees me about it.

MR. SULLIVAN: Yes, sir. He has a memorandum coming over to you tomorrow.

H.M.JR: Tell him and his assistants in the Bureau that if they don't like it, please to keep quiet and come and see me first. I don't want a repetition of the other.

MR. SULLIVAN: Yes, sir.

H.M.JR: I heard Harry White thought it was too tough, but otherwise it was all right. He thought it went too far.

MR. WHITE: No, no. I have some very substantial gripes about it which I presume we will have an opportunity

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to give vent to in the afternoon.

H.M.JR: I can't hear you.

MR. WHITE: I gather from Roy that the presentation has been postponed until tomorrow, before which time I presume there will be an opportunity to raise one or two questions in connection with it.

H.M.JR: You don't--

MR. WHITE: The questions have to be raised with you. They know my view.

H.M.JR: Paul says you wore him out. (Laughter)

MR. BLOUGH: He had a night's sleep since then, Harry.

H.M.JR: Well, those people on the taxes, I can see White, Blough, Kuhn - everybody in the back row. You are not in on that, Huntington?

MR. CAIRNS: No, no.

H.M.JR: Harold, you better come in and see that war bonds are taken care of. Three o'clock.

MR. GRAVES: Yes, sir. I wonder if I could be fifteen minutes late to that. I have Mr. Doob, the publicity director of this motion picture outfit, coming in to see me at three.

H.M.JR: Who?

MR. GRAVES: Mr. Doob, and I think I should see him.

H.M.JR: How do you spell that?

MR. GRAVES: D-o-o-b.

H.M.JR: Sure. You may lose your shirt in those fifteen minutes, but that is your--

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MR. GRAVES: No, I am going to take his.

H.M.JR: On the basis of the result of Saturday night, the radio program was excellent. I congratulate all of you. I have got to the point, I don't care what they do as long as they sell bonds. That is where I have arrived. That is all I have.

MR. THOMPSON: That was a good program.

H.M.JR: The results were wonderful. I will not make any comments on the program, but the results were grand.

MR. KUHN: You made a comment in a telegram to the head of the Blue Network. I hope it is all right.

H.M.JR: What did you say?

MR. KUHN: Wonderful show.

H.M.JR: Do I get a copy of that telegram?

MR. KUHN: Surely.

H.M.JR: Do I ever get copies?

MR. KUHN: They all go over to Miss Chauncey.

H.M.JR: Those with my name, I wish they would go to Mrs. Klotz.

MR. KUHN: Yes, sir.

H.M.JR: Herbert?

MR. GASTON: I don't think I have anything important enough to interrupt the proceedings of today.

H.M.JR: I want to say it was Harry White's suggestion we get out that story yesterday on taxes, for which I again thank him. It was a darned good suggestion of Harry's. It shows the plan is pretty good because he

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has got a couple of reservations. (Laughter)

MR. SULLIVAN: We had some discussion the other day about employing women in the Bureau.

H.M.JR: You have got to talk louder. I have been up in the air.

MR. SULLIVAN: From February first through the last of July we made forty-nine hundred and sixty-two new appointments in the Bureau of Internal Revenue.

H.M.JR: Forty-nine hundred and how many?

MR. SULLIVAN: Forty-nine hundred and sixty-two. Seventeen hundred and seventy-five were men and three thousand one hundred and eighty-seven were women. A hundred and ninety-six were promoted to responsible positions formerly held by men.

H.M.JR: That sounds good.

MR. SULLIVAN: I thought it was a step in the right direction. (Memorandum to the Secretary, dated August 29, 1942, handed to the Secretary.)

Last Friday the Attorney General--

H.M.JR: Excuse me, supposing you give it to me as of the first of September - the vacancies and how many days old they are. Then we will check up on it.

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MR. SULLIVAN: That is what we are getting. I think that all of the vacancies, the thousand and fifty that the Commissioner was worried about, have already been filled, and the pending vacancies are the ones that have occurred within the last three months.

He is preparing just the type of statement you asked for.

H.M.JR: The vacancies and how many days they have been vacant.

MR. SULLIVAN: He never can get that current, Mr. Secretary, because it has to come from all of the districts.

H.M.JR: Well, try it.

MR. SULLIVAN: We will get it as well as we can.

MR. THOMPSON: We get a monthly report.

MR. SULLIVAN: I think the statement I have already asked for will answer your question.

H.M.JR: O.K.

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MR. SULLIVAN: Friday the Attorney General asked for a conference on the work the Bureau is doing to help them in their fight against subversive activities and checking into these different taxes on institutions.

Randolph and I went over and brought over two of the men from the Bureau, and we had a very satisfactory conference. The attitude of the Attorney General and of the Department seems to be entirely changed, and they are now for quality instead of quantity. They had some very practical considerations.

H.M.JR: Good. I also like your silver story, Ferdie.

MR. KUHN: It got a good play. The Times promised to do an editorial correcting themselves. I do not know whether they will.

(Memorandum entitled "Statement of Interview Held with the Honorable Hamilton Fish on August 19, 1942," handed to the Secretary by Mr. Sullivan.)

H.M.JR: How recent is this? I have seen this. Is there a more recent one?

MR. SULLIVAN: That is the last one, sir.

H.M.JR: I will look at it, anyway. Couldn't you summarize it?

MR. SULLIVAN: We can get copies of the agent's recommendations setting forth the facts.

H.M.JR: Could you do that?

MR. SULLIVAN: Yes. I do not think you want to go through this.

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H.M.JR: I don't want it lying around.

MR. SULLIVAN: Mr. Marrs, the head of the technical staff, is going to talk with Mr. Paul. The Commissioner is very much disturbed about the present relief provisions which will require the setting up of a new division in the Board of Tax Appeals to hear special cases on the excess profits tax. He sent a memorandum over to Mr. Paul, and he wanted me to be sure that I brought it to your attention. He was afraid this would threaten the entire decentralized procedure. I talked with Mr. Paul, and he is going to talk with Mr. Marrs. I just wanted to make sure--

H.M.JR: It hasn't registered. You will have to do it again.

MR. SULLIVAN: Well, why don't I wait until after Mr. Paul and Mr. Marrs have had their talk?

H.M.JR: O.K.

MR. SULLIVAN: Right. That is all I have, sir. There are two other matters that I think you are very much interested in, which I will be glad to tell you about whenever you wish to hear about them.

H.M.JR: Viner?

MR. VINER: No.

H.M.JR: Viner, would you get hold of - I want you to travel along with us on this tax on expenditures; and then from Haas, tonight, or whenever he has his memorandum on financing, would you get hold of that? Those two, I think, will keep you busy.

Did you catch any fish?

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MR. VINER: No. The others did, though - a little. I got some good stories, though. (Laughter)

H.M.JR: I want to hear those. What else? He has got a fish story. He knows how to catch them. (Laughter)

MR. KUHN: I hope you read Mr. Merillat's story about the Solomon Islands.

H.M.JR: I read an editorial on it, but I did not read the story.

MR. KUHN: Every paper yesterday played up this six-column story by your Mr. Merillat now a lieutenant in the Marines as the official soldier reporter of the Battle of the Solomons.

H.M.JR: If you will send it in, I will take it home with me.

MR. KUHN: It is great stuff.

H.M.JR: I saw an editorial on him, but I did not see the story.

MR. KUHN: I think the press conference this afternoon, if you have one, would be interested in this as a piece of shop talk on how a tax lawyer can graduate into the by-lines in the newspapers after - I think it is eighteen months or so, if you would be interested in telling them.

MR. SULLIVAN: You can give that another angle, too, about the journalists calling on the other professions to strengthen the ranks. (Laughter)

MR. KUHN: Mr. Paul is going on the air tonight on the Mutual Network to answer the Ruml plan, and a draft has been done by Professor Griswold. I am working it over now.

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H.M.JR: You have had plenty to do the last three days, haven't you?

MR. KUHN: No boredom.

H.M.JR: No boredom - O.K.

MR. GASTON: Beardsley Ruml was pretty much in our corner last night on sales taxes on one of these forums. Did you hear that?

MR. KUHN: I did not hear it, no.

H.M.JR: Well, if Mr. Graves would announce he was going to take a page in every newspaper next week of paid advertising, he would get some good publicity, too, for our tax plan. (Laughter)

MR. GRAVES: Did you see that editorial about the Treasury's advertising policy?

MR. VINER: If you find a way of financing the war without taxes, you will get lots of publicity. (Laughter)

H.M.JR: I am going to raise Ruml. I am going to give away two years.

MR. KUHN: There was an editorial about the Treasury's policy on war-time advertising. Did you see it?

H.M.JR: No.

MR. KUHN: It was very friendly and appreciative.

MR. WHITE: By the newspapers - well, isn't that surprising? (Laughter)

H.M.JR: O.K. What else?

MR. KUHN: That is all.

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H.M.JR: Roy?

MR. BLOUGH: The week-end has not been boring for me either.

H.M.JR: So I gather. How many times did I talk to you and Paul?

MR. BLOUGH: Well, three or four, to my knowledge.

H.M.JR: I think so.

MR. BLOUGH: I hope we didn't bore you.

H.M.JR: No. I hope I made the right decision.

MR. BLOUGH: You will see this afternoon at three o'clock.

H.M.JR: I think what we will do this afternoon - we will have a question and answer and bring out anything that Harry has in his mind. I would like to go through questions and answers myself.

MR. SULLIVAN: May I have a copy of that before so I can go through with it?

MR. BLOUGH: Surely. There are copies available now in mimeograph form. We have not made any distribution yet for very obvious reasons.

H.M.JR: Are you getting nervous? Want to be excused?

MR. GAMBLE: No. We have ten minutes yet.

H.M.JR: You look like you are kind of on the hot seat.

MR. BLOUGH: Are you pretty anxious to have Paul at the meeting at three?

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H.M.JR: No.

MR. BLOUGH: I will see whether he can be spared up there.

H.M.JR: But I would like him here at four for press. I think he definitely should be here.

MR. BLOUGH: Yes.

H.M.JR: You go with me, don't you?

MR. GAMBLE: Yes, sir.

H.M.JR: If he wasn't here he would be squirming downstairs, so he might as well be squirming here. He can't go until I go.

MR. GAMBLE: We all go together.

H.M.JR: We will go around the room, then have a full discussion on this tax plan before we go downstairs. (Laughter) I want to get out myself.

MR. BLOUGH: Everything can wait.

MR. CAIRNS: Mr. Paul sent you a memorandum this morning, a memorandum showing three women attorneys who have had accounting experience.

H.M.JR: Where is that memorandum?

MR. CAIRNS: It came in to you this morning.

H.M.JR: Good.

MR. CAIRNS: That is all I have.

H.M.JR: George?

MR. HAAS: Here is this advisory group. (List handed to the Secretary.)

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H.M.JR: George, will you charge yourself this afternoon - I want to invite in some of the bond people Thursday.

MR. HAAS: Thursday?

H.M.JR: Talk to me at three o'clock this afternoon about inviting in some of these bond people.

MR. HAAS: O.K.

MR. VINER: I didn't know, Mr. Secretary, that they (The band) knew I was coming.

MR. GAMBLE: I have nothing, Mr. Secretary, except to remind these gentlemen that we are all going down together from here at quarter of twelve. We will leave here at quarter of twelve, and they are all to be at the luncheon at two o'clock. They may have to leave the party before it is over downstairs.

H.M.JR: Harry, the next ten minutes are yours.

(Mr. Schwarz entered the conference.)

MR. WHITE: I won't take but a few. I can outshout the band. These are the documents that are ready for the census of American-owned property in foreign countries.

H.M.JR: Hooray! (Laughter)

MR. WHITE: I think I will take this up tomorrow.

H.M.JR: The meeting is adjourned. All right. (Laughter)

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Copy

Treasury Department

TELEGRAPH OFFICE

67

WUWE10 32 GOVT COLLECT NT

TOWD FISHKILL NY AUG 29 1942 1942 AUG 31 AM 7 58

TED GAMBLE

DLR 830 AM MONDAY 31 OFC OF SECY OF TRSY

PLEASE ADVISE NEWSPAPERMEN WHO COVER TREASURY TO ATTEND TWELVE OCLOCK SHOW ON STEPS OF TREASURY AND GIVE THEM RESERVED SEATS. PLEASE TALK TO ME ABOUT JONOTHAN DANIELS. COPY TO MRS KLOTZ.

HENRY MORGENTHAU JR.

752AM AUG 31.

Regraded Unclassified

August 31, 1942

Secretary's reading copy of his remarks at the War Bond Rally sponsored by the Movie Stars as the inauguration of their September drive. The rally was held on the south steps of the Treasury.

Regraded Unclassified

Standing here on the south steps of the Treasury today, I can see thousands of soldiers, sailors and Government workers at this great War Bond Rally. They have come to applaud the motion picture stars who are giving all their time to sell War Bonds during September. Speaking for the Treasury Department I should like to pay my tribute to these actors and actresses, and the entire motion picture industry. They are putting their special talents to work to help win our common victory.

Regraded Unclassified

But this crowd is not all I see from the Treasury building. I can also picture our marines fighting through the jungle in the Solomon Islands, our sailors patrolling the Atlantic sea lanes, our flyers in battle on a dozen fronts around the globe. And I can see millions of our sons and husbands and brothers training in Army camps, from dawn till long after dark, for the hardships and the sacrifices of war.

As we think of this grim effort by our fighting men, let's ask ourselves whether we on the home front are doing all we can to train and toughen ourselves for the coming battles.

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This is going to be a hard war, and it may be a long one. Here on the home front we have not even begun to sacrifice the easy and pleasant and comfortable things of life. We have not even begun to live with the spirit of the American pioneers, who used to say "Eat it up--wear it out--make it do." We have not even begun to scrimp and save, as we shall have to do before this war is won.

Each of us will have to ask himself every morning "What am I personally going to do today to help win this war? What can I give up or do without, so that our soldiers and sailors can have the weapons they need?"

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Remember, the weapons of victory -- the planes and guns and bombs and battleships -- all have got to be paid for. Some of us build them. Some of us will fight with them. But all of us have got to pay for them -- with War Bonds.

The need is great. The time is short. The hour of effort is here. We on the home front must not fall behind our fighting men. We, too, must take the offensive -- now!

Regraded Unclassified

7

73
8/31/42

STARS

16

Edward Arnold
James Cagney
Greer Garson
Bud Abbott
Lou Costello
Red Skelton
Irene Dunne
Hedy Lamarr
Walter Abel
Kay Kyser
Dinah Shore
Ann Rutherford
Virginia Gilmore
Bing Crosby
Ralph Bellamy
Martha Scott

WAR ACTIVITIES COMMITTEE, NEW YORK CITY

Kenneth Thomson, Chairman of the Hollywood Victory Committee

Howard Dietz NO

Si Fabian

6

Francis Harmon

Oscar Doob

Jim Sauter

WAR ACTIVITIES COMMITTEE, WASHINGTON, D.C.

4

Carter Barron
John Payette
Rudolph Berger NO
Sam Galanty

WAR SAVINGS STAFF

3

Carlton Duffus
Robert Harper
Vincent Callahan

29.

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE Aug. 26, 1942

TO MRS. KLOTZ

FROM TED R. GAMBLE

This is the latest list, and I am quite sure, the final one for the Secretary's luncheon on Monday. We could, without too seriously stepping on anyone's toes, eliminate probably four people from this list, but unless it is absolutely necessary, I would suggest that we not do this. I have sent a copy of this list to Mr. Fitzgerald who is arranging for these people to come through the Secretary's entrance for the 11:30 affair on the south Treasury steps. I will be in New York tomorrow, but will be back here Friday morning if there is anything further you want from me.

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE Aug. 29, 1942

TO MRS. KLOTZ

FROM TED R. GAMBLE

This is to advise you that Mr. Dietz and Mr. Berger are unable to attend the Secretary's luncheon on Monday. Mr. Fitzgerald advises us that Mrs. Herrick has been invited, and has accepted.

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Luncheon List

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cceptances:

Gaston — Secretary
Sullivan — Mrs M.
Thompson — Miss Elliot
White — Mrs Herrick
Haas
Graves
Kuhn
Gamble
Schwarz
Viner
~~Klotz~~ — Stephens

let us know
Paul } Both on Hill
Blough }

ll. Odegard. Buffington out of town

Regraded Unclassified

August 31, 1942.
3:30 p.m.

TAXES

Present: Mr. Haas
Mr. Paul
Mr. Friedman
Mr. Shoup
Mr. Blough
Mr. Graves
Mr. Kuhn
Mr. White
Mr. Viner
Mr. Sullivan
Mr. Gaston
Mrs. Klotz

H.M.JR: Where is Roy Blough?

MR. BLOUGH: Right here, sir.

H.M.JR: Well, Roy, supposing you start in and talk and I guarantee you will be interrupted.

MR. BLOUGH: That is fine. What would you like me to do?

H.M.JR: Oh, just start anywhere on this thing.

MR. BLOUGH: Well, I will describe it briefly.

H.M.JR: Was this for tomorrow?

MR. BLOUGH: That is the copy that was done yesterday.

H.M.JR: For tomorrow?

MR. BLOUGH: For tomorrow, and undoubtedly it will be quite different from that by the time we get through.

The fundamental idea is to get a tax on spending

Regraded Unclassified

which would raise a substantial amount of money and at the same time would have a substantial deterring effect on spending.

Now, we started out with the basic idea of a progressive spendings tax, with exemptions.

H.M.JR: Excuse me, did you tell Paul to be here at four o'clock?

MR. BLOUGH: Yes, he will be here.

H.M.JR: Good.

MR. BLOUGH: The more we looked at it the more we saw that it would only get us into some difficulties, because at the lower end of the scale, as we got down farther and farther we had more and more people and we were going to ask them to figure out the spendings tax return; we put it on a quarterly basis, and we were going to have them file quarterly returns. It just did not seem to quite be feasible. On the other hand, if collection at source went into operation we had a good instrument for collecting further income taxes.

So, after a very great deal of trouble, mental trouble, we came to the conclusion it would be better to hitch the spendings tax onto a collection-at-source income tax and, while it is not in here, that would lend itself very well to a certain amount of spendings tax treatment by permitting the deduction of debt payments, insurance, purchase of war bonds, and so on, in arriving at the annual settlement of the taxpayer with the Government for that collected-at-source tax. Aside from that it would not be a spendings tax, but it would be, to that extent, a spendings tax.

Then the question of whether any of it should be paid back came up, and it was decided that we should suggest that some of it be paid back, although that is, I should say, a separate question. It arises out of the feeling on the part of a great many people on the Hill, I am sure, that we are hitting pretty hard at the new taxpayers that we

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are bringing into the picture when we are starting their taxes at nineteen percent, asking them to pay an extra five percent next year, if they were then asked to pay another five percent and have it permanently taken from them.

So that what we have here in this plan is a spendings tax with exemptions of a thousand dollars for single persons, two thousand for married couples, with an additional five hundred for each dependent. Now, that is put in the form of an exclusion, so that everybody who gets more than those amounts will pay on his whole spendings and not merely on the excess of his spendings over the exemptions or the amounts. It is progressive, starting at five percent on the first thousand and going up to a hundred percent over twenty-five thousand dollars. It is perhaps optimistic to expect to get those rates, but those are intended to be very penalizing on spending. It is not to be collected at source but to be collected quarterly, with a very short form indicating spendings, and the tax filed each quarter, and then at the end of the year, filing a return on which the spendings would be computed on the basis of cash receipts and cash disbursements - the money you had available and what you did with it, and everything that was not put into savings and investment and other omitted items counted as spendings.

Hitched onto that, then, is this collection-at-source income tax of five percent with an exclusion of five hundred dollars for single persons, a thousand dollars for married couples, and two hundred and fifty for each dependent, and the exceptions of the income tax would be lowered similarly, and the additional amount of tax not to exceed the amount calculated at the lowest income tax rate. Additional amount of income tax would also be held as a postwar credit for the taxpayer.

Now, without going too much into the reasons why, that is what we came out with. I say in advance, I do not like many elements of it, but I do not know just exactly how to improve it.

Nobody interrupted me, Mr. Secretary, I don't know what is wrong.

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H.M.JR: Well, let's start with John Sullivan.

MR. SULLIVAN: There are two things right off the bat, Mr. Secretary, that disturb me a good deal.

In the first place we are abandoning our position and going right over to a system of compulsory savings.

The other point that disturbs me is that in this memorandum it is contemplated that we will collect this tax through withholding. I think if we start on a straight withholding tax on the income tax, there is going to be difficulty enough.

I think if you confuse it by adding to it an attempt to collect through withholding a spending tax, which nobody in this room will know how to fill out himself without a great deal of research, and we are imposing that on millions of people who have never filed but one straight income tax return - I think we are going to jeopardize the withholding tax, itself. I think we are going to--

H.M.JR: Just a moment, are we - he did all this on the phone with me - are we going to collect this--

MR. BLOUGH: The five percent tax would be collected at source, so far as the employee was concerned, and so far as the employer was concerned, would be indistinguishable during the year, but would then be separated out in the annual return.

There would be a difference in the computation, but as far as we can see - we have made some check on it - it would not be a difficult computation.

MR. SULLIVAN: Then, if that is the way it is done, all you are doing is taking part of the five percent which we now expect--

MR. BLOUGH: No, additional five percent.

MR. GASTON: A total ten percent withholding?

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MR. BLOUGH: That is right.

MR. SULLIVAN: If you are doing that, Roy, you are retarding your effort to finally get your rate of withholding on income tax up where it means something.

MR. BLOUGH: It is possible it may have some effect along that line.

H.M.JR: Before we get to this thing, Roy, I think the important thing to explain to everybody - each person has his own little objections - where is Haas?

MR. BLOUGH: Mr. Secretary, he was out there. He didn't understand you wanted him with this group.

H.M.JR: I said everybody sitting in the back. Explain this - I think it is as important as anything - whatever the income they figure, a hundred and ten, a hundred and twenty - I wish you would explain, before we had this, how much did we reach and how much didn't we reach; and under this proposed plan, how much additional we reach. I think that is the important thing. I mean, to me it is more important than anything else.

MR. BLOUGH: Well--

H.M.JR: Whether you have a withholding tax or anything else.

MR. BLOUGH: With the income tax at the rate brackets, I mean at the exception brackets now contemplated in the Senate discussions, we would have - well, in the House bill we would have a tax base of around thirty-two billion dollars.

H.M.JR: What is your total - what is your figure - a hundred and ten or a hundred and twenty?

MR. BLOUGH: While there may be a hundred and ten billion dollars of total national income, that part that could be considered as available or as get-at-able through taxation is about ninety-six billion dollars.

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H.M.JR: For round figures, call it a hundred billion.

(Mr. Haas entered the conference.)

MR. BLOUGH: So we are getting - our tax base is about thirty-two billion dollars under the income tax which the House has passed.

Now, the income of the people who will be subject to this income tax, but which will be exempted from tax because of personal exemptions, will be about twenty-eight billion dollars more - somewhere in that neighborhood.

In addition to that, there will be somewhere in the neighborhood of thirty-six or thirty-eight billion dollars which will be received by the people who do not file income tax returns.

There has been great objection made to the fact that we are attempting an anti-inflation program by operating primarily, if not exclusively, on the thirty-two billion dollars, which is one-third, about, of the total.

The introduction of a withholding tax, with exclusions instead of exemptions, and which has five hundred dollars, a thousand dollars, and two hundred and fifty, instead of five hundred, twelve hundred, and three hundred, would mean that probably, instead of sixty, possibly sixty-seven or seventy billion dollars, altogether, would come under the income tax in one form or another.

H.M.JR: Let me ask you my way, will you, because you are making it extra complicated. The way the bill passed the House, how much of the hundred odd billion dollars in income would we have reached?

MR. BLOUGH: The tax base would be about thirty-two billion.

H.M.JR: Thirty-two billion - O.K. Now then, does that include or exclude the five percent withholding?

MR. BLOUGH: That excludes the five percent withholding tax - I am sorry, the one now in the House bill, that includes that.

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H.M.JR: And it still remains thirty-two.

MR. BLOUGH: That is right, because the withholding doesn't add anything, in the number of people or their income.

H.M.JR: So it is thirty-two?

MR. BLOUGH: That is right.

H.M.JR: So that excludes sixty-eight billion dollars.

MR. BLOUGH: Roughly two-thirds.

H.M.JR: Now, this suggestion which we are about to make, how much more does that reach?

MR. BLOUGH: That reaches about thirty-five billion more. Does that check with your figures?

MR. FRIEDMAN: Yes.

H.M.JR: Is that right, about thirty-five?

MR. SULLIVAN: But from the same people who had the thirty-two.

MR. BLOUGH: Not altogether, because we are lowering the exemptions substantially.

H.M.JR: It is an additional--

MR. BLOUGH: Most of it comes from the same people, but there will be - well, another seven billion or so from new people.

MR. FRIEDMAN: Five to seven.

H.M.JR: But you are reaching sixty-seven billion out of the hundred billion?

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MR. BLOUGH: Approximately that, yes, sir, "reaching" in the sense that it is part of the tax base.

MR. VINER: You are reaching persons with how much income?

MR. BLOUGH: We are reaching persons now with how much income?

MR. VINER: Yes, under your scheme?

MR. BLOUGH: With about sixty-five or sixty-seven billion dollars.

H.M.JR: You mean numbers of people?

MR. BLOUGH: Persons we reach would have that much income.

H.M.JR: You are reaching another seven million taxpayers; that is the figure?

MR. BLOUGH: We will tax approximately seven million more taxpayers.

H.M.JR: I mean there are all kinds of "shadations" on this thing, but the main thing when we sat around here and discussed this thing was that the criticism they can levy at us correctly is that we are only reaching one-third of the national income, and that does not do much of a job as an anti-inflation measure. Then we come along and roughly add another third.

MR. GASTON: I just don't understand why that is true.

MR. SULLIVAN: No, Mr. Secretary, the seven million additional people you are adding are because of the reduction of the exemptions on your personal income tax, and it is entirely exclusive of anything in the expenditure tax, isn't that so, Roy?

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MR. BLOUGH: That is this additional withholding tax.

MR. SULLIVAN: That is right, and you are not getting one dime from anybody under the expenditure tax who is not being taxed under the income tax law.

MR. BLOUGH: One dime is a rather small amount; I should say we are getting certainly more than one dime, but you are right in general.

MR. SULLIVAN: Certainly less than one percent.

MR. BLOUGH: The expenditure tax, per se, without reference to this additional tax at the bottom, has higher exemptions than our income tax.

MR. SULLIVAN: The income tax is twice as high; and if a person who is exempt from an income tax today earns twice as much as he now earns, he will still be exempt from the expenditure tax.

MR. BLOUGH: That is approximately correct, but that, of course, is in order to keep the Bureau of Internal Revenue from collapsing under the load of administering the expenditure tax, not because we wanted it that way.

H.M.JR: Let me say something. I don't want to be unfair, but, John, you sat here the night we discussed that thing from eight to ten and didn't say anything. Now suddenly you seem very much excited, and I don't understand it.

MR. SULLIVAN: I am not excited at all; I never saw this memorandum until this afternoon, Mr. Secretary.

MR. GASTON: This is an entirely new plan.

MR. KUHN: This is not what we discussed Wednesday, Mr. Secretary.

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MR. BLOUGH: May I indicate the differences between what this is and what we discussed on Monday?

H.M.JR: Go ahead.

MR. BLOUGH: The difference is this: What we discussed on Monday was a split plan in which the first two thousand dollars - up to two thousand dollars of income, or up to twenty-five hundred dollars, we would assume a man spent all of his income and therefore it was a tax on his income, and not on his spendings, and above that we would tax him on his spendings.

Now we tried to hitch that together, to take the bottom and add it to the top for the same man, tax the bottom as income, assuming his expenditures are the same, and take the top as true expenditure tax. The things didn't fit together, and we tried every which way to get them to fit together. We finally decided they wouldn't fit together, so we did exactly the same thing as was proposed here; we treated the people at the bottom on their incomes and not on expenditures, but we ran the tax all the way up so as to avoid the notch proposition. To that tax we could very well allow deductions for savings and bond purchases and insurance, make it something of an expenditures tax; and then we added on a true expenditures tax at the levels that we were talking about, making the true expenditures tax here that night. So far as the number of people involved, and so far as the treatment of the bottom incomes are concerned, it is exactly the same as we talked about that night, but we could not splice them together. We had to make it in the form of two taxes. That is the only difference.

H.M.JR: We did mention it that night.

MR. SULLIVAN: That night there was--

H.M.JR: The fact that it is exclusion and that we would tax the people--

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MR. SULLIVAN: That is right, that was discussed here that night.

H.M.JR: What wasn't discussed here?

MR. SULLIVAN: Well, Mr. Secretary, you asked me for my comments and I told you there were two things that stood out here; one was our abandoning our position on compulsory savings.

H.M.JR: We are not abandoning it. I explained this thing. I mean, Harold - I brought Harold and Ted Gamble in here and I explained to them that we were going to have a post-war credit on the lower-income group, and we can't collect it because we can't collect forty million income tax returns, so we are going to exclude thirty-three million of them and give it to them in the form of a post-war credit amounting to about five percent. Didn't I explain that before I went away?

MR. GRAVES: Yes.

H.M.JR: I explained that before I left, didn't I? It was Thursday or Friday.

MR. GRAVES: Yes.

H.M.JR: And, Roy, we haven't changed from that.

MR. SULLIVAN: I was not familiar with that development.

H.M.JR: I tell you, John, I am not going to apologize to anybody. I cannot go around and see every single person in the Treasury. I mean, that is Paul's and Blough's job to do the explaining. I did personally explain it to Graves and Gamble because I know they are not tax people, they are selling bonds. I wanted their advice. That is why he is here today. I wanted to explain to him what the plan was as I saw it. But if the rest of the thing hasn't been explained, it is somebody else's responsibility, not mine.

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MR. BLOUGH: May I say this, that on last Monday night the post-war credit feature was very definitely discussed, and it was the unanimous opinion of the people outside the Treasury that that was a good idea. It wasn't discussed here.

H.M.JR: I mentioned it Monday night, and I mentioned it Tuesday morning. We discussed it with George and then I took the trouble to explain it to Graves and Gamble to get their reactions.

But that is your objection to the thing, the post-war credit?

MR. SULLIVAN: Those are the two things that struck me in the first place. The other thing is on page eight where we argue the difference - where we argue a comparison between this and the sales tax. If this is the statement that is going up there, I think that that should be omitted.

H.M.JR: Well, I tell you what you do; if the men - my press conference won't last very long. I think there should be a meeting in Paul's office, if he has the time, or Blough's office, because Paul is going on the air tonight. This same group should meet and discuss it - I mean, rather than take it out on me, take it out on each other. Then I can see you tomorrow.

MR. SULLIVAN: I wasn't trying to take it out on anybody.

H.M.JR: I am not being personal, John. I mean Harry White hasn't gotten started yet. I mean, I am very definitely not being personal, but I am just thinking of what way we could save time. If these people - they didn't come to a decision until about six o'clock yesterday. When this was written, God only knows. It must have been written during the night. By the looks of Roy I should say that he did it last night, during the night.

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MR. BLOUGH: No, Mr. Secretary, it had been going on for several days, and once we made the final decision the rest of it was relatively simple.

H.M.JR: I feel this way, if not everybody in this room is not satisfied - I am sure they are not - as far as I am concerned it is not as important as it is to get a plan out and get it before the Committee, even if the plan is only seventy-five percent perfect. We just couldn't sit here - White came to me Friday and said we had to do something, that we can't be shoved around by some new man coming in, and why doesn't the Treasury do something. White didn't say that, but that was the inference, that we had to get something out or be accused of not being a leader, and instead being a follower.

So I insisted that we get something out, and here it is. I think, considering that we only started to discuss this a week ago Saturday night and the boys really only had a chance to work on it Friday and Sunday - I think they did a very good job. Now, there may be things, but there is nothing I have heard yet that disturbs me; so I think we had better - there is no use my getting - I mean, Paul may have to do his radio speech. Could you do a little listening, or can't you take any more today?

MR. BLOUGH: Oh, sure, Mr. Secretary, I am as fresh as a daisy after your little party here.

H.M.JR: Then I want you to stay at the press conference; and as soon as it is over, the people in the room will be notified. Harold does not have to stay unless he wants to. Do you want to stay, Harold?

MR. GRAVES: No, I don't think so, unless you want me to.

H.M.JR: You understand it, don't you?

MR. GRAVES: Yes, sir.

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H.M.JR: Do you want to say anything about it?

MR. GRAVES: No.

H.M.JR: I personally think that your interests and my interests are well taken care of. I think if this thing would pass in seventy-five percent of its form - if it is passed, that leaves the people with a lot of money which they are going to save rather than spend and pay a tax; then you and I go after those people for the money they have got left and give them a post-war credit of five percent. We will have to adjust the plan and give them an allowance for what is taken on our ten-percent plan. We would have to give them an allowance, because a lot of people and a lot of money - and I expect to continue the volunteer program, modified, to take care of this, but I expect to keep it just the same.

MR. GRAVES: I wonder if it wouldn't be helpful, Mr. Secretary, if Mr. Blough were to prepare again the schedules which he prepared under the other proposal showing as to the people in different income brackets, the aggregate amount that they would have to pay. Do you know what I mean, Roy?

MR. BLOUGH: Yes.

MR. GRAVES: Wouldn't that be a helpful thing to do?

MR. BLOUGH: I would be very glad to do it.

(Mr. Paul entered the conference.)

H.M.JR: What we are going to do is this: A lot of people here haven't seen this, and I have told them you will have to work after press on your radio talk, won't you?

MR. PAUL: I just finished that, subject to one little change.

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H.M.JR: I thought Roy could take them on after this is over. A number of them have suggestions.

MR. PAUL: Are we going to go into the details of this?

H.M.JR: I am not.

MR. PAUL: Is anybody? I talked to George about it, and it seems to me that no details should be given out to the press before we give them out to the Committee. So we held it over until tomorrow. At my request of George, we held it over because we were not quite ready, and I think - what do you think, John? George said this definitely - he said, "I think it would be better not to give anything out to the press until it is before the Committee."

H.M.JR: At four o'clock, that suits me.

MR. BLOUGH: You had in mind the meeting with this group afterwards?

H.M.JR: Then if that is the case, you and Paul had better not be here. Paul and Blough had better not be here at my four o'clock press conference.

MR. PAUL: I think you ought to be very general and say it is not customary to give out any statements, out of respect to the Committee, and you are going to hold all comment until the plan is presented to the Committee, which will probably be tomorrow.

H.M.JR: There is only this thought, Randolph. I wondered if you could not hold a school for the press so that when they hear it tomorrow they would understand it. That would be a tremendous advantage - not to print anything.

MR. PAUL: Then the thing to do would be to take them in a room and hold a school and have no release.

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H.M.JR: That is right, but I think that that would be a tremendous advantage.

MR. BLOUGH: We would prefer to wait until there are any changes.

MR. WHITE: That rules out, Mr. Secretary - and maybe it will be ruled out anyhow, but there is one major change that I should like to argue for, and I should hate to see it ruled out before we even start; unless you can make it in such general terms that such changes as I have in mind are not ruled out, it kind of stops us from putting any change in after it is once gotten out.

H.M.JR: All right, we will do this: We will say nothing to the press. Do you agree with me, Herbert?

MR. GASTON: Yes.

MR. KUHN: Well, Senator George was perfectly willing and glad to have the press told tomorrow that as soon as the Executive session was over they could come to the Treasury and get the whole thing from Randolph Paul, and I think that it might be--

MR. PAUL: He was strong for giving them an adequate explanation, but he doesn't want to do it before, and I think some of the Committee would resent it if we gave it out.

MR. KUHN: It might be a good idea to tell them you can't do it before the Committee meeting, but that you can assure them for Senator George and yourself that as soon as this is given to the Committee they can get a full discussion of it here at the Treasury.

H.M.JR: Let's leave it this way - are you too tired to take this group on now?

MR. PAUL: No, I can do it. I want Roy with me, because I am not up on the plan. It has been twenty-four hours since I saw it.

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H.M.JR: Why don't you finish your speech for tonight first?

MR. PAUL: If Roy takes them on, I will circulate in there a little bit. Roy was working on it yesterday.

MR. BLOUGH: If there are to be changes in it you certainly ought to be there.

H.M.JR: He has got to finish his speech.

MR. PAUL: That is all done, except the first paragraph.

H.M.JR: Where should they meet? I want to get them out.

MR. PAUL: Is Room 220 being used now?

H.M.JR: They can have my poster room across the hall, or Bell's room is empty. Meet in Bell's room. Do you want to go there now?

MR. BLOUGH: Do you (Paul) want to stay here for the Ruml plan? They will probably ask questions about that.

H.M.JR: You don't want to be here. If you are here, then you have got to answer a lot of questions. I won't have to answer any.

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Statement of Randolph E. Paul, General Counsel of the Treasury Department, before the Senate Finance Committee in Executive Session, on the Treasury plan for a spendings tax and collateral measures

The great need for revenue has been stressed by the Treasury Department throughout the consideration by Congress of this tax bill. Recommendations for rates higher than those appearing in the House bill were made in all the major taxes, including individual income, corporation, estate and gift, and excise taxes. Those recommendations were reaffirmed by Secretary Morgenthau in his statement before this Committee and there has been no cause for any substantial change in them.

To an increasing extent in recent weeks, expanding individual incomes have been exerting pressures on prices and the cost of living. At the same time, the supply of consumer goods and services has been dwindling rapidly in the face of our tremendously accelerated war production. This points clearly to the necessity of resolute action along more than one front, including the enactment of a tax program well above even the $8.7 billion of additional revenue originally recommended by the Treasury.

The large increases in taxation which we need at this time to combat inflation should, insofar as possible satisfy the following requirements:

1. The taxes should operate to withdraw purchasing power. Moreover, insofar as practicable they should actually discourage consumer spending since the pressure of income on prices and the cost of living results from the effort to spend purchasing power.

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2. The burden of the tax and the pressure it exerts should be very light on the millions whose standard of living in many cases is inadequate to support productive efficiency and decent living. The burden should increase as the standard of living rises so that the pressure will be the greatest on those elements of spending which are least necessary to the individual and to the war effort.

3. The tax, being an addition to existing taxes, should not interfere any more than is absolutely necessary with the meeting of commitments to pay debts, purchase insurance, and make regular savings, which were undertaken at lower tax levels.

4. The tax should not make more difficult the exercise of direct price controls, rationing, and other methods of inflation.

5. The tax should be reasonably capable of administration in the light of its importance as an anti-inflationary and revenue measure.

The Treasury has come to the conclusion that these requirements would be most nearly met by a three-point combined program.

1. A progressive tax above exemptions would be imposed on the spendings of individuals for consumption goods and services.

2. A refundable tax would be imposed on the total incomes of persons whose incomes exceeded $500 for a single person, $1,000 for a married couple, and $250 for each dependent.

3. To integrate the regular income tax with the refundable tax, the exemptions of the income tax would be reduced to $500, $1,000, and $250, and the increase in tax occasioned thereby would be held as a post-war credit to the account of the taxpayer.

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1. The spendings tax

The proposed spendings tax is directly aimed at the control of expenditures on goods and services. Its major features are as follows:

a. Tax base: The tax would be levied at progressive rates on total expenditures for consumer goods and services. That is, the tax base would be the same as under a retail sales tax except that it would include expenditures on services as well as on tangible goods.

b. Persons liable to spendings tax: The tax would apply only to persons spending more than specified amounts on consumer goods and services. Single persons would be excluded from the tax if they spent less than $1,000, married couples if they spent less than $2,000, and the exclusion would be increased an additional $500 for each dependent. These amounts represent exclusions, not exemptions. Persons subject to the tax would be taxed on all of their spendings.

c. Computation of the tax base: The amount of spendings would not be computed directly, but would be derived indirectly by subtracting from the total amount of funds at the disposal of the taxpayer the amounts used for purposes other than current consumption. The major nontaxable uses of funds are repayment of debt, premiums paid on life insurance, expenditures for the purchase of bonds or other capital assets, gifts and contributions, and payment of taxes. The attached schedule lists the items that would have to be obtained to compute the total funds at the disposal of the consumer and the total nontaxable use of funds (Exhibit 1).

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d. Method of collection: The liability under the spendings tax as under the income tax cannot be determined until after the close of the year in which spendings took place. However, collection of the tax would not be delayed until the ultimate liability was determined.

The tax would be collected currently by requiring individuals to report the approximate amount of spending at short intervals, say quarterly, with a final adjustment after the close of the year. The quarterly report might contain no more than a single item - approximate amount of spending during the preceding quarter - or might contain a more detailed statement.

e. Tax rates: The tax rates would be progressive. The tax on the spendings of each single person would be as follows:

Spendings	Tax rate
\$ 0 - \$ 1,000	5%
1,000 - 2,000	15
2,000 - 3,000	25
3,000 - 5,000	40
5,000 - 10,000	60
10,000 - 25,000	80
25,000 and over	100

The direct application of this progressive spendings tax schedule to a family as a unit would be unduly harsh on the larger families and would favor single persons, since, the larger the family, the greater is the necessary amount of spendings and the higher the rate at which the spendings would be taxed. This difficulty can be overcome by putting the family's tax on a per capita basis. The family's total

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spendings would be divided by the number of persons in the family. The progressive rate schedule would be applied to the resulting per capita spendings. The per capita tax computed in this way would be multiplied by the number of persons in the family to get the total family tax. For this purpose, a dependent child would be counted as equivalent to one-half a person.

For example, a married couple with one dependent would comprise 2.5 taxable spendings. If this family spent $5,000, spendings per taxable person would be $2,000. According to the above rate schedule, the tax would be $200 per person, or $500 for the family. Married couples would be permitted to file either joint returns or separate returns. This would not lead to any discrimination under this method of computing spendings per taxable person.

In order to avoid large differences in tax between persons just below the exclusion limits and persons just above, persons just above the exclusion limits would be permitted to pay an alternative tax equal to the difference between their spendings and the exclusion amount.

The amounts and effective rates of tax under the above rate schedule are shown in Exhibits 2 and 3.

f. Effective date of tax: The spendings tax would be made effective as of August 31, 1942. It is essential that this be done in order to prevent any buying in anticipation of the enactment of the spendings tax. In addition, unless the spendings tax is made effective as of the

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date on which it is announced, an opportunity will be given to individuals to convert their bank deposits into currency thereby hoping to have spendable funds upon which an adequate check cannot be made. These and similar problems can be entirely prevented only by making the spendings tax effective as of August 31, 1942.

2. The Refundable Tax.

The refundable tax is designed to reach the lower levels of spending that cannot easily be reached by the spendings tax.

a. Tax base: The tax would be levied on total net income from all sources. The same deductions would be allowed as under the regular income tax except that no exemptions would be allowed.

b. Persons liable to the tax: The tax would apply only to persons with incomes above certain specified amounts. Single persons would be excluded from the tax if their income was less than $500, married couples if their income was less than $1000, and the exclusion would be increased an additional $250 for each dependent. These amounts represent exclusions, not exemptions. Persons subject to tax would be taxed on all their income.

c. Method of collection: The ultimate liability under the refundable tax could not be computed until after the close of the year. However, the tax would be collected at source from wages, salaries, and dividends in the same manner as it is proposed to collect part of the regular income tax. Collection at source with respect to this tax and with respect to the regular income tax would be combined into a single

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item so that the two taxes combined would involve no greater problems for employers and payors of dividends than the collection at source heretofore proposed.

d. Tax rate: The refundable tax would be levied at a rate of 5 percent on all of income. The amounts so collected up to a maximum of $500 per year would be refunded to the taxpayer after the war, without interest. The amount collected in the first year of operation of the tax would be refunded in the first year following the close of the war; the amount collected in the second year would be refunded in the second year following the close of the war, and so on.

If the Committee believes that this additional 5 percent refundable tax will mean too high a combined tax rate on the highest brackets of income, an appropriate adjustment can be made in the rates of the regular income tax.

In order to avoid large differences between the tax of persons just below and just above the exclusion limits, the tax on persons just above the exclusion limits would be limited to half of the excess of their income over the exclusion amount.

3. Reduction of exemptions for the regular income tax.

The proposed exemptions for the regular income tax involve the lowering of the exemption for married persons by $200 below the amount tentatively adopted by the Committee and for each dependent by $50. It is proposed that the resulting increase in taxes be treated as a

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post-war credit to be refunded in the same manner as the refundable tax described above. The amount of tax to be refunded would be computed on the reduction of exemptions at the combined normal and first bracket surtax rate, that is, at 19 percent under the rates tentatively adopted by the House. This will simplify the computation and will make the post-war credit of equal value throughout the income scale.

4. Comparison with alternative tax measures.

The sales tax has been urged as a means of accomplishing the anti-inflationary objectives of this program. The suggested program, however, does not have the serious disadvantages of a sales tax. The sales tax bears heaviest on those who can least afford to pay it. A spendings tax can provide exclusions and, equally important, can be enacted at progressive rates so as to make unnecessary spendings increasingly costly. This is impossible under a sales tax without at the same time levying an intolerable burden on the great masses of the people. A spendings tax therefore permits a more selective control of expenditures than is possible under a sales tax.

The refundable tax likewise can provide exclusions and the fact that it is refundable within limits means that the burden will be only for the period of the war and not permanent.

It has not been found practicable, moreover, to impose sales taxes on the sales of numerous kinds of services. For administrative reasons,

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it is generally necessary to limit the sales tax to sales of tangible goods. This leaves exempt a large fraction of spending. A spendings tax would reach spendings for both tangible goods and services. The sales tax takes no account of differences in personal situations and is therefore more likely than a spendings tax or a refundable tax to stimulate concerted efforts to secure higher wages.

A sales tax, especially at the wholesale and manufacturing levels will enter into some costs of production and therefore make price control difficult. In addition, it is likely to affect parity prices for farm products. Even if the tax is imposed at the retail level, these difficulties are not entirely obviated. A spendings tax has neither of these effects since it is collected directly from individuals.

The Treasury Department has already asked for higher individual income tax rates and believes that these rates do not represent the limit that can be obtained from the income tax. Further increases in individual income taxes have, however, been strenuously objected to on the grounds that persons with fixed incomes would not be able to meet their commitments for debt repayment, insurance premiums, and other fixed obligations, even though such expenditures have little or no inflationary effect. The spendings tax by exempting such outlays is not subject to this objection. Moreover, the spendings tax puts a direct penalty on spendings compared with saving and is therefore more effective in reducing consumer expenditures than an equal amount withdrawn

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from purchasing power through an income tax. If rates are graduated steeply enough the expense of consuming beyond a certain amount can be made almost prohibitive.

The spendings tax would not be suitable for use in normal times, because it permits the accumulation of wealth without the payment of a tax and thus is much inferior to the income tax in measuring ability to pay taxes. In times like the present, however, it can serve as an important element in the fiscal system. It cannot replace a steeply graduated income tax but it can supplement it.

Like any new tax, the spendings tax necessarily involves administrative and compliance problems of no small magnitude. These problems are somewhat reduced by the fact that the spendings tax can be administered along with the income tax. Nevertheless it will create a serious administrative problem in securing compliance, in checking information not now required on income tax returns, in educating the public to an entirely new type of tax, and in helping the public to fill out the forms which they will be required to submit. Compared with other measures of comparable importance in meeting the inflation and revenue problems, however, the administrative difficulties should not prove disproportionately large. In time of war, administrative difficulties cannot be allowed to stand in the way of measures vital to the nation's welfare.

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Exhibit 1.

The Spendings Tax Return

(To be made part of income tax return)

Funds at the disposal of the consumer

1. Salaries, wages, and other compensation for personal services... $
2. Dividends and interest received, including government interest..
3. Rents, royalties, annuities, pensions..........................
4. Withdrawals from business, profession, partnerships, trusts.....
5. Cash receipts from gifts, bequests, and insurance...............
6. Receipts from sale of capital assets............................
7. Receipts from repayment of loans made to others.................
8. Receipts from borrowing, including debts incurred on installment purchases.......................................
9. Cash and bank balances at beginning of year.....................
10. Other receipts..
11. Total disposable funds (items 1 to 10).................. $

Deductions: Non-taxable use of funds

12. Cash and bank balances at end of year......................... $
13. Cash gifts and contributions..................................
14. Interest and taxes paid, except on owner-occupied homes.........
15. Expenditures on the purchase of capital assets..................
16. Life insurance premiums, annuity, and pension payment...........
17. Outlays for repayment of debt, including installment debt.......
18. Loans made to others..
19. Other nontaxable disbursements..................................
20. Total deductions (items 12 to 19).................. $

21. Expenditures subject to tax (item 11 minus item 20)............ $

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Exhibit 3.

Amount of spendings tax and tax as a percent of spending, for selected amounts of spending

Total spendings	Single person No dependents		Married couple No dependents		Married couple Two dependents	
	Amount of tax	Effective rate	Amount of tax	Effective rate	Amount of tax	Effective rate
$ 1,000	0	0	0	0	0	0
1,200	80	6.7	0	0	0	0
1,400	110	7.9	0	0	0	0
1,600	140	8.8	0	0	0	0
1,800	170	9.4	0	0	0	0
2,000	200	10.0	0	0	0	0
2,500	325	13.0	175	7.0	0	0
3,000	450	15.0	250	8.3	0	0
3,500	650	18.6	325	9.3	225	6.4
4,000	850	21.2	400	10.0	300	7.5
5,000	1,250	25.0	650	13.0	450	9.0
6,000	1,850	30.8	900	15.0	600	10.0
8,000	3,050	38.1	1,700	21.2	1,100	13.8
10,000	4,250	42.5	2,500	25.0	1,750	17.5
15,000	8,250	55.0	5,500	36.7	3,750	25.0
20,000	12,250	61.2	8,500	42.5	6,750	33.8
25,000	16,250	65.0	12,500	50.0	9,750	39.0
50,000	41,250	82.5	32,500	65.0	28,750	57.5

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Exhibit 2

Spendings tax: - Rates and amount of tax

Expenditure per taxable person	Tax rate	Cumulative tax per taxable person
$ 0 - 1,000	5%	$ 50
1,000 - 2,000	15	200
2,000 - 3,000	25	450
3,000 - 5,000	40	1,250
5,000 - 10,000	60	4,250
10,000 - 25,000	80	16,250
Over 25,000	100	---

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TREASURY DEPARTMENT
Washington

FOR RELEASE, MORNING NEWSPAPERS
Tuesday, September 1, 1942
8/31/42

Press Service
No. 33-2

The following address by Randolph E. Paul, General Counsel for the Treasury Department, is scheduled to be broadcast over the Mutual Network at 9:15 p. m., Eastern War Time, Monday, August 31, 1942.

Last Friday you may have heard over this network a discussion of the so-called pay-as-you-go tax plan by its sponsor, Mr. Beardsley Ruml. There is no doubt that the plan he has advanced is original and ingenious. The Treasury has considered it earnestly and with the great respect to which it is entitled, both on the merits and because of the high standing of its author. But that consideration has not led us to the conclusion that the plan should be adopted. I should like to outline to you tonight the reasons why the Treasury does not like the plan.

Mr. Ruml proposes to put all taxpayers on a current basis by skipping a year's tax. Under his plan the tax liability for the year 1941 will be simply forgiven by the Government. The payments which have been made during this year 1942 for that year's tax will instead be treated as current payments on 1942 tax liability. Of course 1942 income will not ordinarily be the same as 1941 income, so when March 1943 comes around, each taxpayer will file a return for 1942 showing what his actual 1942 income was. If it was more than the amount his payments covered, he will then pay the difference in tax. If it was in fact less, he will be entitled to a refund. And his return of 1942 income will also be treated as a tentative return for 1943 which will determine his advance or current payments of 1943 tax liability.

The description I have just given illustrates some of the Treasury's objections to the Ruml plan. In the first place it is extremely complicated. Each year's tax payments will depend upon two returns instead of one as at present. The taxpayer will first file a return of one year's income which will be the tentative return for the following year. He will pay tax according to this return, and then when the year is ended he will have to file another return showing what his income actually was, and he will then have to make a further payment or collect a refund depending on how his income varied. The administrative problems for the Government in collecting these additional payments and in making a large number of refunds would be very great, and the system would certainly be very confusing for many taxpayers.

Another objection is the fact that the Ruml plan, despite its label as the pay-as-you-go tax plan, would not in fact put taxpayers current with their tax liability to the Government. Many taxpayers experience considerable fluctuations in their annual incomes. In their cases the

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Ruml plan would not be a pay-as-you-go plan at all. Let's take the case of a man who ordinarily makes about $3,000 a year, but who puts through a successful deal in one year so that he makes $10,000. Under the Ruml plan he would pay on a $3,000 income in the year he had $10,000, and then in the following year when he had an income of $3,000 again, he would have to pay a deficiency on his last year's tax, and then pay currently on the basis of a $10,000 income. His tax payments for that year would in fact exceed his total income for that year, and his problem would be a very serious if not impossible one. The Ruml plan does not in fact achieve its basic purpose to put the income tax on a current basis; its seductive allure is in fact an illusion.

Why, then, has the Ruml plan been so earnestly advanced and so assiduously pushed forward? We can find much of the reason when we turn to consider the Treasury's third objection to the scheme. It is an essential part of the Ruml plan that one year's taxes be forgiven. It is said that this treats everyone alike; everyone is given a clean slate for 1941. But let us see how this works out. In the first place several billions of dollars of tax liability are cancelled. That is a somewhat surprising way to raise tax revenue in wartime. And what is the result of treating all alike? From eighty to ninety percent of the taxpayers have incomes below $3,000, and they would be forgiven from a few dollars up to a maximum of two or three hundred dollars each. But the wealthy man with an income of half a million dollars would save a tax liability of more than $350,000.

If 1941 were a normal year the plan would be bad enough, but 1941 was not a normal year in any sense of the word. It was a year in which our factories made more shiny new cars, more bright gadgets of all kinds, more goods for consumer use than in any year in our history. Individuals made a great deal more money last year than they are apt to do now with the impact of rationing, growing scarcities, higher taxes, and other effects of the war. Under Mr. Ruml's plan such individuals would pay no tax on their 1941 earnings at all. The man who got huge commissions for placing war contracts in 1941 would pay no tax at all. The man who profited by manufacturing as many civilian goods as the traffic would bear would pay no tax at all. Anyone who had a large income for 1941 — and that goes for thousands, if not millions, of people — would get a wholly fortuitous tax windfall.

This hardly seems to be treating everyone alike. It is instead the passing out of huge benefits to those who need them least, and at a time when we must be getting more revenue instead of giving it away.

It is true that taxpayers would keep on paying year after year under the Ruml plan, and the loss of revenue would not actually appear until a taxpayer's income declined or until he died. But it is undeniably true that over a period of years the Ruml plan involves giving away a sum of billions of dollars, and giving it largely to the wealthy taxpayers who

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need it least. It is not surprising, therefore, that it has been energetically pushed by those who benefited by some of 1941's better than usual incomes.

With the basic purpose of the Ruml plan the Treasury has much sympathy. It would be fine if a substantial part of our income tax liability could be put on a current basis. The easiest way to do this is to collect the basic part of the tax at the source, that is, to withhold it from wages, salaries, interest and dividends. The difficulty in the way of putting such a plan into full operation has lain in the fact that it would involve a double payment of tax liabilities in the same year, first the tax on last year's income, and second the tax on this year's income which would be withheld at the source. The Ruml plan points a way by which this difficulty can be eliminated. It would make it possible for us to introduce now a comprehensive system of collection at the source which would, in fact, put the great majority of our taxpayers on a current basis, with the tax collected week by week from their incomes as they receive it.

We have already suggested to the Senate Finance Committee a plan whereby the pay-as-you-go principle would be applied to all normal taxes and to the first bracket of surtaxes. This would put at least eighty percent of our taxpayers on a current basis. But the plan as Mr. Ruml proposed it, is not acceptable for the three reasons which I have outlined. It is a very complicated scheme; it would not, in fact, put the taxpayers on a current basis; and it involves forgiving a year's tax liability, with the greatest benefit going to those of the biggest incomes.

It is an attractive idea to get square with Uncle Sam; Mr. Ruml himself has made great use of that word "square" in arguing for his plan. But it is not enough to be square. In our American vocabulary, the phrase is "fair and square". It is our deep conviction at the Treasury that the Ruml plan is not fair and square. Until it can be made fair, we at the Treasury will not take the responsibility of recommending it to the Congress and to the taxpayers of America.

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August 31, 1942
3:31 p.m.

Lewis Douglas: Hello, Henry.

HMJr: Hello, Lew?

D: I'm sorry to bother you.

HMJr: You haven't.

D: But I - I wanted to get this - put this question to you.

HMJr: Yes.

D: You know we - the Maritime Commission had an arrangement with Canada....

HMJr: Yes.

D: ....under the terms of which the Canadian shipyards were to build certain ships for us. Now that agreement expired, and the deliveries under that contract are going to terminate very shortly.

HMJr: Yes.

D: They have a capacity up there to produce about eighty-one ships.

HMJr: Yes.

D: Could we have the green light to go ahead and negotiate such a contract for them to....

HMJr: Well, Lew, without trying to put you to too much trouble, I couldn't have a sort of an informal note on it saying how much it amounts to and over how long a period?

D: Well, it will extend through forty-three, and eighty-one boats, deliveries beginning in January....

HMJr: Yes, but just so I - I'll not keep it more than twenty-four hours.

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D: Fine, Henry, I'll get it off to you this afternoon.

HMJr: If you get it off to me and mark it "Special", I promise not to keep it more than twenty-four hours.

D: I will do that, Henry.

HMJr: But there's several people here I'd like to show it to.

D: All right, old man.

HMJr: How's that? Will that twenty-four - would twenty-four hours embarrass you?

D: Not a bit, Henry. That's wonderful.

HMJr: Okay.

D: Thank you, old man.

HMJr: Thank you.

D: Thank you ever so much. Goodbye.

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August 31, 1942
4:32 p.m.

HMJr: Hello.

Operator: Mr. Patterson.

HMJr: Hello.

Robert P. Patterson: Hello.

HMJr: Henry talking.

P: Yes, Henry.

HMJr: Sorry we couldn't have lunch with you Sunday.

P: That's all right.

HMJr: But we didn't have enough notice.

P: You didn't have much notice.

HMJr: No. Bob, I just want to tell you I'm still sitting here waiting for the Army to tell me how much of that special currency you want.

P: Well, I understood that Carter was to get in touch Friday....

HMJr: Yeah.

P: ....with Bell's man....

HMJr: Yeah.

P: ....and - and order about ten million....

HMJr: Well, he hasn't....

P: ....and in denominations that they were going to discuss.

HMJr: Well, he - up to three minutes ago, he hasn't done it.

P: I'll get after it.

HMJr: And we're still waiting -- and they've been talking -- but we're still waiting and they've increased it to twenty million dollars and we're still sitting here waiting and I didn't

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HMJr: (cont.)	want - I hope when you get down to it that you'll let General Eisenhower know that it wasn't that we - who delayed it.
P:	I know, I will.
HMJr:	So he won't be cussing me out over there.
P:	I - I'll - I'll get right after it.
HMJr:	I'm serious about that. I don't want him to think that - that I've been sitting here holding up the Army.
P:	Who is Bell's man?
HMJr:	Just a minute, I'll ask. (Talks aside) Who is Bell's man? Batchelder.
P:	Batchelder?
HMJr:	Yes.
P:	Right.
HMJr:	He's the man, and - but they've been in contact with him, but we still don't have the formal order, and I thought you'd like to know this.
P:	Yes, yes, that's right.
HMJr:	I thank you.
P:	Thank you. Goodbye.

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Delivered in person by Col. Foster
on September 1, 1942 at 10:15 a.m.

The work of printing the currency willprobably be finished on Thursday, but the War Department does not know when they will need it. All they want is to have it ready when they ask for it.

The Bureau is working a double shift.

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SECRET Rec'd from Col Fosters hands 9/1/42 at 10:15 am (Sept 1, 1942)

August 31, 1942.

The Honorable,

The Secretary of the Treasury.

Dear Mr. Secretary:

Reference recent conversations on a special occupational currency, it is requested that the Treasury print immediately $20,000,000 of this specially marked currency.

The denominations of this special currency and the details as to its delivery to Army agencies will be arranged for separately with your office by the Chief of Finance of the Army.

Sincerely yours,

ROBERT P. PATTERSON,
Under Secretary of War.

SECRET

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orig to Mr Heffelfinger
8/31/42.

August 31, 1942.

Honorable Henry Morgenthau, Jr.,
Secretary of the Treasury.

Dear Henry:

General Carter tells me that his people are consulting with Mr. Batchelder of the Treasury Department today and that an order for the currency will be given today.

Sincerely yours,

Robert P. Patterson
Under Secretary of War.

RPP:er

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Prepared by: Mr. Conrad
Mr. Sandelin
Mr. Turner
Mr. Tickton
Mr. Murphy
Mr. Haas

RY DEPARTMENT

FICE COMMUNICATION

DATE August 31, 1942

TO Secretary Morgenthau

FROM Mr. Haas

Subject: September Financing

SUMMARY

(1) Banking institutions have absorbed 41 percent of the increase in the total interest-bearing debt so far this year. The proportion of the increase in the debt taken by banking institutions varies widely from quarter to quarter, depending upon various special circumstances.

Commercial banks, both inside and outside of New York City, are likely to take substantial proportions of the September financing. Insurance companies have greatly depleted their cash resources by subscriptions to the August reopening of the "tap" issue, and probably will be out of the market for the most part during September.

(2) At least $3 billions will have to be raised in the September financing, and it would seem desirable to offer two issues. As vehicles for the financing, a 2-year, 6-month, 1-1/4 percent note and a 5- to 7-year, 1-3/4 percent bond are suggested.

(3) There are reasons for believing that the regular types of market securities are more attractive to the average individual investor than the long-term "tap" issue. The traditional methods of offering market securities make it very difficult to appeal to this demand effectively, however. Certain technical innovations are suggested, therefore, which would make possible the application of some selling pressure in connection with the September financing and clear the deck for the use of more intensive selling methods later on.

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I. <u>Who Is Purchasing the Current Increase in the Public Debt?</u>

During the period between the beginning of the year and August 22, the total interest-bearing public debt increased by $21.4 billions. Of this amount, 41 percent was absorbed by banking institutions -- i.e., commercial banks and the Federal Reserve Banks. This compares with 28 percent absorbed by such institutions during the preceding 9 months.

During the same period, the increase in the <u>marketable</u> debt was $13.4 billions, of which 66 percent was absorbed by banking institutions. During the preceding 9 months, the increase in the marketable debt had been only $4.8 billions, of which 67 percent was absorbed by banking institutions.

The above figures and many others are shown in the following table and in the attached chart which analyze the absorption of the increase in the public debt since March 31, 1941 (the commencement of the Treasury Survey of the Ownership of Government Securities):

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Absorption of the Increase in the Public Debt
April 1, 1941 - August 22, 1942 *

	Total Debt		Marketable Debt Only **	
	Increase (billions of dollars)	Absorbed by banks*** (percent)	Increase (billions of dollars)	Absorbed by banks*** (percent)
1941				
Apr. 1 - June 30	2.3	61	1.1	129
July 1 - Sept. 30	3.0	8	0.3	85
Oct. 1 - Dec. 31	6.0	26	3.4	46
Apr. 1 - Dec. 31	11.3	28	4.8	67
1942				
Jan. 1 - Mar. 31	3.8	15	1.0	54
Apr. 1 - June 30	8.9	49	6.0	72
July 1 - Aug. 22	8.7	45	6.4	62
Jan. 1 - Aug. 22	21.4	41	13.4	66

* August 1942 figures are partly estimated.

** Excludes marketable obligations held by Government agencies and trust funds; includes depositary bonds and long-term "tap" issue.

*** i.e., by commercial banks and Federal Reserve Banks; excludes mutual savings banks.

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It will be noted that the proportion of the debt absorbed by banks varies widely from quarter to quarter, depending upon special circumstances, such as the number of financings during the quarter, the opening and reopening of the long-term tap issue, the seasonal distribution of sales of savings bonds, and the institution of new types of securities such as tax savings notes.

The following comments with respect to the present absorptive capacity of several classes of investors appear pertinent:

(1) Commercial banks outside of New York City have been important purchasers of market issues of Government securities during the entire period covered by the chart, and it is a reasonable expectation that they will continue to be so in the immediate future.

(2) Commercial banks in New York City were largely out of the market for Government securities from May 1941 through March 1942. Since the latter month, they have been fairly liberal purchasers of Government securities, as a result of which they ran down their excess reserves from \$956 millions on April 1 to \$178 millions on August 19, just before the recent decrease in reserve requirements in central reserve cities. The reserve position of these institutions has now been re-established in a small way by the decrease in reserve requirements, and they probably may be counted upon to subscribe to new issues of Government securities to the limit of their ability.

(3) Insurance companies subscribed to \$762 millions of the August reopening of the tap issue. As the total cash holdings of 36 large life insurance companies amounted to only \$876 millions on July 31, it is a reasonable expectation that these companies will be largely out of the market during September.

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(4) Individuals subscribed to $214 millions of the 2 percent bond issued in July and to $188 millions of the 2 percent bond issued in May. As allotments to individuals (including preferred allotments) probably amounted to about 50 percent in both cases, bonds actually sold to individuals amounted to about $100 millions for each issue. As discussed in Section III of this memorandum, individuals are an important potential outlet for marketable Government securities, but can probably be reached only by an intensive selling effort.

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II. What Issues Should Be Used For The September Financing?

At least $3 billions will have to be raised in the major September financing. In order to raise this amount of money, it would seem desirable to divide the financing into two issues. The following table presents a sampling of what can be done at the present time in each of the principal maturity sectors of the market. The indicated premiums are, of course, approximate.

	Estimated Yield Basis*	Probable Price
	(Percent)	
3/4 percent certificate due May 1, 1943 (7-1/2 months)	.65	100.065
1-1/4 percent note due March 15, 1945 (2 years, 6 months)	1.21	100-3/32
1-1/2 percent note due December 15, 1946 (reopening) (4 years, 3 months)	1.48	100-3/32
1-3/4 percent bond due September 15, 1947-49 (5 years - 7 years)	1.70	100-8/32
2 percent bond due December 15, 1949-51 (reopening) (7 years, 3 months - 9 years, 3 months)	1.98	100-4/32
2-1/4 percent bond due March 15, 1954-57 (11 years, 6 months - 14 years, 6 months)	2.22	100-10/32

* Based on closing bid prices, August 29, 1942.

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As vehicles for the September financing, the 2-year, 6-month, 1-1/4 percent note and the 5- to 7-year, 1-3/4 percent bond listed in the preceding table are suggested. Neither of these issues falls in a maturity sector which has been used recently. The market for each of them has had a "rest" and ought to be good. Both issues bear fairly low rates of interest and fit in reasonably well with the "pattern of rates."

Consideration is suggested in Section III of this memorandum of certain technical innovations in the manner of offering securities in the September and later financings. If the September financing is to be carried out on traditional lines, however, it might well consist of $1.5 billions each of the two issues mentioned in the preceding paragraph.

The following remarks appear pertinent with respect to the other issues listed in the table:

(1) The 3/4 percent certificate, due next May, might be substituted for either of the issues just suggested. It is believed preferable, however, that this be held in reserve for a "quickie" financing in late September or early October to tide over the working balance until the proceeds of the regular October financing are available. Such an issue could be put out on a few days' notice, as it is more closely analogous to a bill offering than to a regular financing. If the May certificate maturity is not held in reserve in this manner, it might be advisable to raise substantially more than $3 billions in the September financing.

(2) The 2 percent bond listed in the table is a reopening of an existing issue. While such a reopening is by no means an impossibility, it does not seem as advisable at the present time as the use of an entirely new issue. Two percent bonds, furthermore, have been "worked" rather

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heavily of late and deserve a "rest".* It would seem desirable, in any event, to reserve the use of a 2 percent bond for the next financing, particularly if a major popular appeal is to be made at that time as discussed later in this memorandum.

(3) The 1-1/2 percent note listed in the table is also a reopening of an existing issue. It should be noted, in addition, that a 1-1/2 percent note would fit in better in a joint offering with a 2 percent bond than with either a 1-1/4 percent note or a 1-3/4 percent bond, however, and the issuance of a 2 percent bond at the present time seems inadvisable for the reasons just stated.

(4) A 2-1/4 percent bond would doubtless be extremely popular. Its non-use at the present time is suggested on the basis of broad policy considerations. If a 2-1/4 percent bond were offered, it would be absorbed largely by commercial banks. Its higher rate would increase the interest burden on the public debt, while its longer maturity would increase the possible strain on the banking system after the war. As such, it appears a bad bargain for the Treasury, and its use is not suggested despite the widespread demand for it.

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* In our opinion, this point may easily be over-emphasized. If all issues placed with the banks are to be held within a 10-year maturity range and the cost of such financing held to the lowest practicable level, intensive use must be made of all securities with a coupon rate of 2 percent or less. It is interesting to note in this connection that bank purchases of Government securities in Great Britain are confined almost entirely to Treasury bills, Treasury deposit receipts and 2-1/2 percent bonds. The latter bonds fall in almost exactly the same maturity range as do 2 percent bonds in this country.

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III. Suggested Technical Innovations

The net demand deposits of all member banks are now in excess of $40 billions. The velocity of circulation of these deposits is near the record low. A large proportion of them are held by individuals, and it seems reasonable to suppose that, if they could be reached, they should provide an important market for Government securities. While the sale of Government securities to individual holders of large balances would not reduce current consumption, it would help to check the rise in bank deposits. Such sales would, therefore, occupy a position, as far as the problem of controlling inflation is concerned, intermediate between sales of bonds to bona fide new savings and sales to banks.

An attempt has already been made to reach these funds by means of the long-term "tap" issue. This attempt has not been very successful. (Total sales to individuals amounted to only $26 millions in May and $36 millions in August.) It has been suggested that the regular types of marketable Government securities might receive a better reception among individual investors if a real sales effort was made in this direction. This suggestion seems reasonable inasmuch as the large amount of idle demand deposits now held by individuals would appear to indicate that they are more concerned with liquidity than with income. It is further supported by the fact that purchases by individuals of the last two 2 percent bonds (about $100 millions per issue) have been substantially greater than their purchases of the "tap" security.

An intensive selling effort devoted to fully marketable securities in the 1-1/4 to 2 percent maturity range might, therefore, prove more fruitful than it has been in the case of the restricted "tap" issue. Such an intensive sales effort would be very difficult, however, within the framework of the present methods of offering marketable Government securities.

The organization of a selling effort requires considerable time. A real selling job of the type suggested is, therefore, probably impossible in September. It is

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suggested, however, that certain technical innovations might be made in connection with the September financing which would facilitate some selling effort at that time -- sort of a "reconnaissance in force" -- and would make the mechanics of Government security offerings more suitable for the application of greater sales pressure later on.

The suggested innovations are as follows:

(1) The financing should be open to banks for only two days, but to other investors for several days thereafter. (It should be noted that a precedent has been set for such action by the previous practice of holding an issue open a day or two for subscriptions of up to $25,000 after the books have been closed for larger subscriptions.)

(2) The total amount to be raised by the two issues should be stated, but the proportion of such amount to be allotted to each issue should be left to the determination of the market.

(3) All subscriptions by non-banking investors and subscriptions by commercial banks up to $25,000 should be allotted in full.

(4) Subscriptions by commercial banks in larger amounts than $25,000 should be allotted so as to divide the amount of the total financing not taken up by preferred subscriptions between the two issues in the same proportion as the total allotted subscriptions for such issues. This would mean that the percentage allotments of the two issues would be equal, and the total amount of each security issued would be in accordance with the preference of the market. All bank subscriptions of over $25,000 for either issue would, of course, be allotted at least $25,000.

If the financing were carried out along the lines above suggested, the Victory Fund Committees would have more time in which to work and would be able to offer their customers firm merchandise, rather than an uncertain prospect of allotment. The approximate amount of bank subscriptions might

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be announced as soon as closed, and would provide an effective selling point to the Committee salesmen in convincing their prospects that the merchandise was fairly priced. The banks, on their part, while they would have only a second call on the deal as a whole, would at least have their choice of the security which they desired.

It should finally be noted that, while a plan such as that just discussed would permit the more effective reaching of non-banking investors, the enthusiastic cooperation of the banks would be an indispensable condition for its success. There are two obstacles which might possibly stand in the way of this cooperation. These are (1) the natural reluctance of the banks to "play second fiddle" to non-banking subscribers in the matter of allotments, and (2) the fear of individual banks that they will lose deposits as a result of sales to non-banking subscribers. While both of these obstacles are worthy of consideration, it is believed that they can be overcome.

With respect to the first obstacle -- the reluctance of the banks to "play second fiddle" -- it is probable that they may be made to see rather easily that preferential allotment to non-banking subscribers is implicit in any attempt to place debt outside of the banking system. Furthermore, in addition to the patriotic motive of the banks for supporting such an attempt, they have the consolation that the prospective debt increase is of such a magnitude that there "will be enough for all."

The second obstacle -- the reluctance of individual banks to lose deposits -- is somewhat more difficult to handle. It is true, of course, that the banking system as a whole does not lose deposits as a result of sales of Government securities to non-banking investors, but individual banks may and will lose deposits as a result of the distribution of specific issues. This is a consequence, of course, not of the innovations suggested here, but of any attempt to sell Government securities outside of the banking system. Deposit losses as a result of a particular issue will occur only in a minority of the banks, however, and in the vast majority of these the deposits so lost will be more than offset by the general increase of deposits incident to the expansion of bank holdings of Government

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securities. In view of this and of the general interest of the banks in non-inflationary war financing, it is probable that such deposit losses as would occur in individual institutions would be accepted with good grace.

As the cooperation of the banks is so vital to the success of any plan for the sale of Government securities outside of the banking system, it is, of course, suggested that any proposed move in that direction be thoroughly canvassed with the banking profession before being placed in operation.

Attachment

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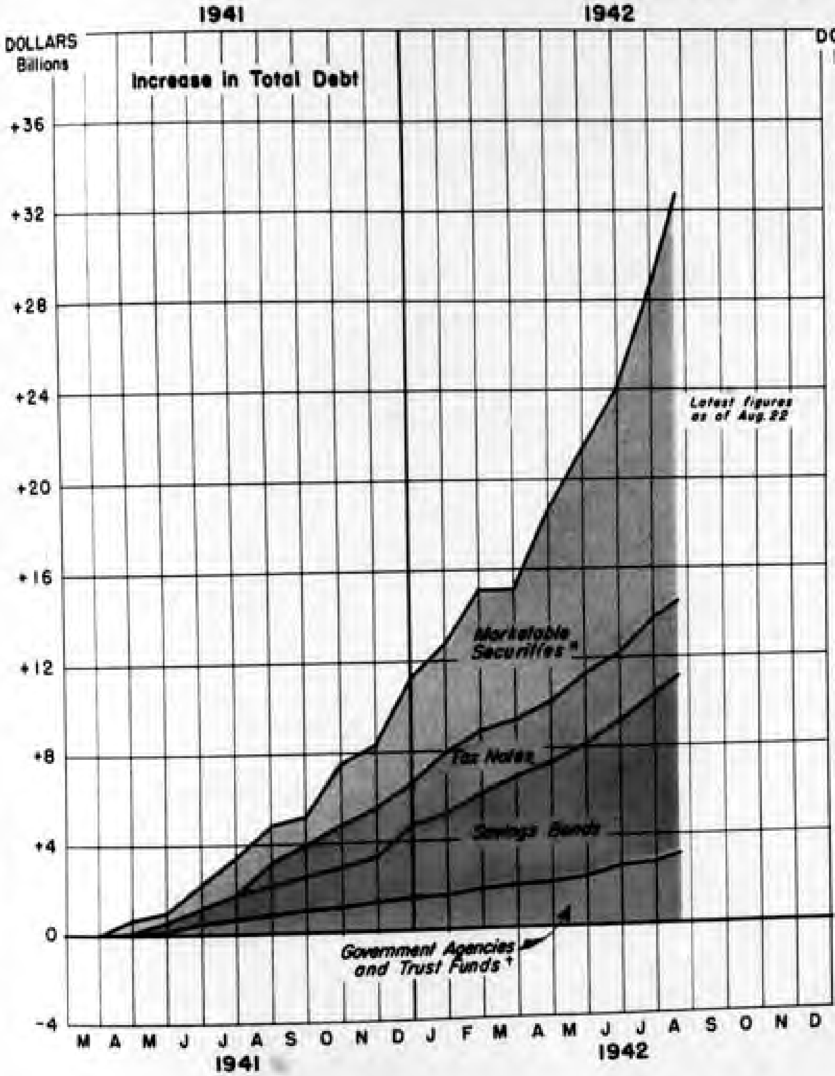
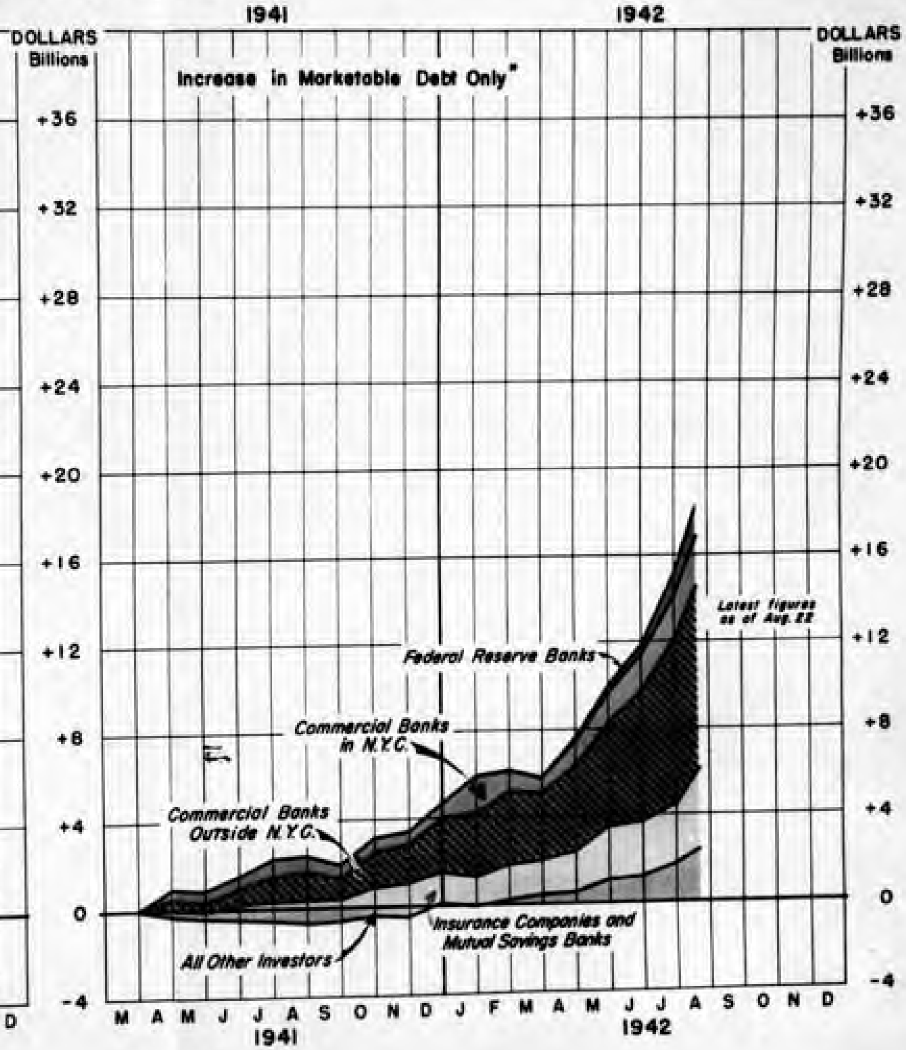
ABSORPTION OF THE INCREASE IN THE INTEREST-BEARING PUBLIC DEBT SINCE MARCH 31, 1941





* Excludes those held by Government Agencies and Trust Funds; includes Depositary Bonds.
† Includes Adjusted Service Bonds.

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

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE August 31, 1942

TO Secretary Morgenthau

FROM Mr. Haas

Subject: Analysis of Replies Received to Telegram on Tax Notes

In accordance with your request, we have analyzed the replies received to your telegram of August 27, requesting the opinions of the presidents of the Federal Reserve Banks with respect to certain proposed changes in the present series of tax notes, and your letter of the same date requesting the opinion of the Board of Governors on this matter.

It appears from comments in the telegrams received from the banks that the Board of Governors wired its reply to your letter to the Federal Reserve Banks. Mr. Sproul sent in a reply in his capacity as Vice Chairman of the Executive Committee of the Federal Open Market Committee in addition to his reply as President of the Federal Reserve Bank of New York, stating in the former that the Executive Committee of the Federal Open Market Committee "is body within the Federal Reserve System with which Treasury has maintained primary contact on Treasury financing problems."

All of the replies received approved the changes suggested in the terms of the Series A Tax Notes.

The Board of Governors, Mr. Sproul in his capacity as Vice Chairman of the Executive Committee of the Federal Open Market Committee, and ten of the twelve Federal Reserve Banks urged that the interest rate on the Series B Tax Notes should be on a graduated scale. The two replies not urging such a scale (those from the Atlanta and Cleveland banks) were the first two received.

Except for the matter of the graduated scale, all of the proposed changes in the Series B Tax Notes were generally commended, except that one bank (San Francisco)

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advised against use of the tax notes as security for loans, feeling that the redemption feature provided sufficient liquidity, and recommended that no interest be allowed on cash redemptions unless the notes had been held for a full year. Two banks, on the other hand, (Minneapolis and St. Louis) especially commended the proposal to make the Series B Tax Notes eligible for collateral, the Minneapolis bank suggesting that this feature be extended to the Series A Notes.

The Minneapolis bank also suggested that it might be desirable to limit the sales of the new Series B Tax Notes to $100,000 annually per holder and issue a new Series C Note with no limitation on holdings. The latter series would have the same features as the Series B Notes, except that it would bear a lower graduated rate of return.

Copies of the communications sent to the Federal Reserve Banks and the Board of Governors and of the replies received are attached hereto.

Attachment

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TREASURY BILLS

	Sept. 2	Aug. 26	Aug. 19	Aug. 12
Amount offered	$350 M	$350 M	$350 M	$350 M
Bids tendered	873	892	712	594
Low rate	.297%	.297%	.297%	.293%
High rate	.372	.372	.376	.376
Average rate	.367	.369	.372	.372
Amount in New York	$147 M	$139 M	$155 M	$188 M
Amount in Chicago	67	106	72	99
Amount in San Francisco .	25	22	25	21
Amount in balance of country	111	83	98	42

August 31, 1942

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UNITED STATES SAVINGS BONDS - TOTAL

Comparison of August sales to date with sales during the same number of business days in July and June 1942

(At issue price in thousands of dollars)

Date	August daily sales	Cumulative sales by business days			
		August	July	June	August as percent of July
August 1942					
1	$ 26,267	$ 26,267	$ 28,418	$ 29,539	92.4%
3	38,765	65,032	52,687	45,442	123.4
4	27,023	92,055	79,964	67,046	115.1
5	25,835	117,890	126,495	98,208	93.2
6	40,450	158,341	157,605	132,341	100.5
7	38,184	196,524	201,056	154,085	97.7
8	24,218	220,742	240,974	192,659	91.6
10	41,021	261,763	288,729	206,523	90.7
11	15,274	277,037	324,856	236,552	85.3
12	24,724	301,761	372,020	259,772	81.1
13	22,757	324,518	402,122	281,724	80.7
14	28,504	353,022	435,929	303,163	81.0
15	12,830	365,852	467,599	334,398	78.2
17	41,806	407,659	505,257	345,497	80.7
18	14,551	422,209	527,186	368,782	80.1
19	27,756	449,965	580,443	387,369	77.5
20	23,791	473,756	602,129	414,804	78.7
21	22,187	495,943	636,640	429,158	77.9
22	13,246	509,189	670,075	468,812	76.0
24	41,029	550,219	703,062	485,338	78.3
25	19,667	569,885	722,572	510,446	78.9
26	25,385	595,271	776,393	533,097	76.7
27	23,275	618,546	806,228	554,915	76.7
28	23,861	642,406	839,266	575,657	76.5
29	18,031	660,438	869,209	609,516	76.0

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

August 31, 1942.

Source: All figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds.

Note: Figures have been rounded to nearest thousand and will not necessarily add to totals.

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UNITED STATES SAVINGS BONDS - SERIES E

Comparison of August sales to date with sales during the same number of business days in July and June 1942

(At issue price in thousands of dollars)

Date	August daily sales	Cumulative sales by business days			
		August	July	June	August as percent of July
August 1942					
1	$ 14,044	$ 14,044	$ 15,821	$ 19,834	88.8%
3	22,178	36,222	30,701	27,841	118.0
4	14,575	50,797	47,523	40,811	106.9
5	12,988	63,785	77,320	58,199	82.5
6	23,004	86,789	95,044	82,988	91.3
7	24,959	111,748	116,643	98,197	95.8
8	16,429	128,176	139,390	125,245	92.0
10	26,805	154,981	164,161	134,157	94.4
11	9,885	164,866	183,238	154,242	90.0
12	15,921	180,787	209,787	169,920	86.2
13	16,356	197,143	225,532	186,470	87.4
14	18,760	215,903	243,938	201,700	88.5
15	9,578	225,481	261,766	225,684	86.1
17	28,683	254,163	284,111	233,218	89.5
18	9,737	263,900	296,344	249,033	89.1
19	17,650	281,550	327,712	261,321	85.9
20	15,525	297,075	339,951	280,742	87.4
21	16,026	313,101	358,135	291,729	87.4
22	9,881	322,982	376,396	321,114	85.8
24	30,522	353,504	394,984	331,806	89.5
25	13,692	367,195	405,679	347,673	90.5
26	16,107	383,303	438,256	362,550	87.5
27	14,932	398,234	455,706	378,505	87.4
28	17,328	415,563	473,962	392,224	87.7
29	12,177	427,740	488,173	417,117	87.6

August 31, 1942.

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

Source: All figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds.

Note: Figures have been rounded to nearest thousand and will not necessarily add to totals.

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UNITED STATES SAVINGS BONDS - SERIES F AND G COMBINED

Comparison of August sales to date with sales during the same number of business days in July and June 1942

(At issue price in thousands of dollars)

Date	August daily sales	Cumulative sales by business days			
		August	July	June	August as percent of July
August 1942					
1	$ 12,222	$ 12,222	$ 12,597	$ 9,705	97.0%
3	16,587	28,810	21,986	17,601	131.0
4	12,448	41,258	32,441	26,235	127.2
5	12,847	54,105	49,175	40,009	110.0
6	17,447	71,552	62,561	49,353	114.4
7	13,225	84,777	84,413	55,888	100.4
8	7,789	92,566	101,585	67,414	91.1
10	14,216	106,782	124,568	72,366	85.7
11	5,389	112,171	141,618	82,310	79.2
12	8,803	120,974	162,232	89,852	74.6
13	6,401	127,375	176,590	95,254	72.1
14	9,744	137,119	191,991	101,464	71.4
15	3,253	140,372	205,833	108,715	68.2
17	13,124	153,496	221,147	112,279	69.4
18	4,814	158,309	230,842	119,749	68.6
19	10,106	168,415	252,731	126,048	66.6
20	8,266	176,681	262,178	134,062	67.4
21	6,161	182,842	278,505	137,429	65.7
22	3,365	186,207	293,679	147,698	63.4
24	10,507	196,715	308,077	153,532	63.9
25	5,975	202,690	316,893	162,774	64.0
26	9,278	211,968	338,137	170,547	62.7
27	8,343	220,311	350,522	176,410	62.9
28	6,532	226,844	365,305	183,433	62.1
29	5,854	232,698	381,036	192,398	61.1

ffice of the Secretary of the Treasury,
Division of Research and Statistics.

August 31, 1942.

ource: All figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds.

Note: Figures have been rounded to nearest thousand and will not necessarily add to totals.

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Sales of United States savings bonds
August 1 through August 29, 1942
Compared with sales quota for same period
(At issue price in millions of dollars)

Date	Series E				Series F and G				Total			
	Actual sales: Daily	Actual sales: August 1 to date	Quota, August 1 to date	Sales to date as % of quota	Actual sales: Daily	Actual sales: August 1 to date	Quota, August 1 to date	Sales to date as % of quota	Actual sales: Daily	Actual sales: August 1 to date	Quota, August 1 to date	Sales to date as % of quota
1	$ 14.0	$ 14.0	$ 16.0	87.5%	$ 12.2	$ 12.2	$ 7.7	158.4%	$ 26.3	$ 26.3	$ 23.7	111.0%
3	22.2	36.2	47.3	76.5	16.6	28.8	21.5	134.0	38.8	65.0	68.8	94.5
4	14.6	50.8	61.0	83.3	12.4	41.3	29.6	139.5	27.0	92.1	90.6	101.7
5	13.0	63.8	84.0	76.0	12.8	54.1	45.4	119.2	25.8	117.9	129.4	91.1
6	23.0	86.8	107.3	80.9	17.4	71.6	58.7	122.0	40.5	158.3	166.0	95.4
7	25.0	111.7	134.4	83.1	13.2	84.8	68.8	123.3	38.2	196.5	203.2	96.7
8	16.4	128.2	154.1	83.2	7.8	92.6	76.3	121.4	24.2	220.7	230.4	95.8
10	26.8	155.0	190.6	81.3	14.2	106.8	87.9	121.5	41.0	261.8	278.5	94.0
11	9.9	164.9	205.1	80.4	5.4	112.2	94.1	119.2	15.3	277.0	299.2	92.6
12	15.9	180.8	227.1	79.6	8.8	121.0	105.1	115.1	24.7	301.8	332.2	90.8
13	16.4	197.1	247.9	79.5	6.4	127.4	114.0	111.8	22.8	324.5	361.9	89.7
14	18.8	215.9	271.0	79.7	9.7	137.1	120.9	113.4	28.5	353.0	391.9	90.1
15	9.6	225.5	287.7	78.4	3.3	140.4	126.4	111.1	12.8	365.9	414.1	88.4
17	28.7	254.2	319.2	79.6	13.1	153.5	135.8	113.0	41.8	407.7	455.0	89.6
18	9.7	263.9	332.2	79.4	4.8	158.3	141.3	112.0	14.6	422.2	473.5	89.2
19	17.6	281.6	353.0	79.8	10.1	168.4	151.9	110.9	27.8	450.0	504.9	89.1
20	15.5	297.1	373.6	79.5	8.3	176.7	161.0	109.8	23.8	473.8	534.6	88.6
21	16.0	313.1	397.4	78.8	6.2	182.8	168.3	108.6	22.2	495.9	565.7	87.7
22	9.9	323.0	415.1	77.8	3.4	186.2	174.3	106.8	13.2	509.2	589.4	86.4
24	30.5	353.5	449.0	78.7	10.5	196.7	184.8	106.4	41.0	550.2	633.8	86.8
25	13.7	367.2	462.9	79.3	6.0	202.7	191.0	106.1	19.7	569.9	653.9	87.2
26	16.1	383.3	484.5	79.1	9.3	212.0	203.0	104.4	25.4	595.3	687.5	86.6
27	14.9	398.2	505.0	78.9	8.3	220.3	213.2	103.3	23.3	618.5	718.2	86.1
28	17.3	415.6	527.8	78.7	6.5	226.8	221.4	102.4	23.9	642.4	749.2	85.7
29	12.2	427.7	544.2	78.6	5.9	232.7	228.1	102.0	18.0	660.4	772.3	85.5
31			575.0				240.0				815.0	

Office of the Secretary of the Treasury, Division of Research and Statistics. August 31, 1942.

Source: Actual sales figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds. Figures have been rounded and will not necessarily add to totals.

Note: Quota takes into account both the daily trend during the week and the monthly trend during the month.

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August 31, 1942

MEMORANDUM FOR THE PRESIDENT:

In accordance with your request of August 27, I am attaching hereto draft of a letter to Senator Murray for your signature.

(Signed) H. Morgenthau, Jr.

By Secret Service Agent
9/1/42 9:08 a.m.

File to Thompson
Photo NMC

Regraded Unclassified

August 31, 1942.

Dear Jim:

I am glad that you have called my attention to the hardships that may be suffered by many small businesses as a result of the war effort. The problem is one that has concerned me for some time, and I wish very much that a solution might be found.

I notice that Senator Pepper has introduced a bill creating a corporation for the relief of such small businesses. It would be helpful to me to know what you and your committee think of this bill, and what, if any, changes in it might be needed to make it workable and successful.

In the meantime I am sending a copy of your letter to the Secretary of Commerce, the Secretary of the Treasury, the Chairman of the Board of Governors of the Federal Reserve System, and the Chairman of the War Production Board, with the request that they do everything they can to cooperate with the work of your committee.

Very sincerely yours,

Hon. James E. Murray,
United States Senate,
Washington, D. C.

FK/lk

Regraded Unclassified

THE WHITE HOUSE
WASHINGTON

August 27, 1942.

MEMORANDUM FOR THE

SECRETARY OF THE TREASURY

FOR PREPARATION OF REPLY
FOR MY SIGNATURE.

F.D.R.

Regraded Unclassified

JAMES E. MURRAY, MONT., CHAIRMAN
MALONEY, CONN. ARTHUR CAPPER, KANS.
ELLENDER, LA. ROBERT A. TAFT, OHIO
MEAD, N. Y.
STEWART, TENN.

United States Senate

Special Committee to Study Problems of
American Small Business

THE WHITE HOUSE
AUG 26 8 56 AM '42
RECEIVED

August 24, 1942

Honorable Franklin D. Roosevelt
The White House,
Washington, D. C.

My dear Mr. President:

This is a matter which, in spite of the tremendous burdens you are now bearing, I consciensciously believe should have your earnest consideration.

Our Senate Small Business Committee is receiving an ever increasing amount of complaint from small business men throughout the country who have mortgages and other forms of indebtedness falling due this year and are being pressed for settlement in full.

For the most part, these obligations appear to be held by local institutions and especially banks. You can well understand how these demands present almost an impossible situation for most small businesses. Yet, from the complaints received, there is evidence of a growing panic on the part of financial institutions, who, undoubtedly, in normal times, would renew these obligations without very much difficulty.

It is my fear that this condition may grow to tremendous proportions with disastrous possibilities for the country as a whole, to say nothing of its effect upon hundreds of thousands of small business enterprises.

I feel sure that you would want the situation brought to your attention. I am taking this means of doing so now. I have recently addressed a communication to Jesse Jones, with reference to the same matter, but have, as yet, had no reply from him on it.

Very sincerely yours,

James E. Murray
Chairman

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COPY FOR: Miss Chauncey

141

Distributed to: Secretary
Secretary's Files
Mr. Bell
Mr. B.Bernstein
Mr. E. M. Bernstein
Mr. Blough
Mr. Cairns
Mr. Foley
Mr. Gaston
Mr. Glasser
Mr. Graves
Mr. Hass
Mr. Johnson
Mr. Odegard
Mr. Paul
Mr. Pehle
Mr. Southard
Mr. Sullivan

FROM: MR. WHITE

Regraded Unclassified

August 31, 1942

MEMORANDUM FOR THE FILES

A meeting was held in Mr. White's office on August 27, 1942, at 3:45 p.m., to receive the delegates presented by Senator Green of Rhode Island, including Mr. C. W. Handy, Mr. Ed C. Mayo, Mr. Edward O. Otis, Mr. G. A. Ingleby, and Mr. F. A. Balleau, Jr. Present for the Treasury were Mr. White, Mr. B. Bernstein, and E. M. Bernstein.

Mr. Mayo, who is the head of Gorham's, stated that the problem of the silversmiths was to secure enough silver for current work until they have had time to convert into war industry. His firm, Gorham and Company, was already 60 percent converted and in six or nine months more would be fully converted. He said that perhaps the provision of 50 million ounces of the Treasury's silver stock to the trade in the next six months would be sufficient to keep most fabricators going until they could convert.

Mr. Ingleby indicated that the problem of the smaller fabricators was somewhat more difficult. In general, they were only some 30 or 40 percent converted to war work and many of the smaller plants were in no position to take on war orders. Nevertheless, there was no question, he said, of trying to perpetuate a non-essential industry. All that was asked was enough silver to give those who could convert into war work an opportunity to do so.

Senator Green emphasized the importance to the war effort of keeping these fabricators operating. Many of them have trained people to do war work and it is essential that they keep their organizations going until they acquire war orders. It would be a waste of real skills to force these people out of business now.

Mr. B. Bernstein inquired what plan they had for getting Treasury silver into the silver market. Mr. Mayo suggested that it could be done by executive order or by a short bill, a copy of which he left with Mr. B. Bernstein.

Mr. White said that the Secretary's position has always been that nothing in the Treasury's jurisdiction should be done that would impede the war effort. As far as silver goes, the Treasury has put all of its free silver stocks into the war effort, making it available to industrial plants where silver could be used for non-consumptive purposes in place of copper. Mr. White added that we are trying to put every ounce

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Division of Monetary
Research

of silver that is available into the market. To that end we are going to sell our 5 million ounces of silver ordinary, and we have put pressure on the Swedes which will result in their selling 500,000 ounces which they had been holding off the market.

Senator Green reverted to the point that all that was desired was to keep these silver fabricators going and to prevent their staffs from disintegrating during the period of preparation for conversion to war work.

Mr. White pointed out that the problem of proper distribution of silver in the market as among the various producers was, of course, under W.P.B. jurisdiction. Senator Green replied he appreciated the Treasury's attitude, but wished to make certain the Treasury would not oppose their attempts to get enough silver to keep the plants going during the transition period.

Mr. White suggested that if they wished to prepare a report on the employment, degree of conversion, expected conversion, and the amount of silver needed by the silver fabricators, he would be glad to examine it. Mr. White concluded again that the Treasury's position was that everything should be done to further the war effort and that this applied to the silver industry as well as to all of the industries.

E. M. Bernstein

Regraded Unclassified

August 31, 1942

Dear Henry:

Despite the fact that I solicited your very kind note concerning my speech, I want you to know that I am deeply appreciative of what you have said about it.

Sincerely,

Claude

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

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Treasury Department 14
Division of Monetary Research

Date Sept. 8 1942

o: Secretary Morgenthau

This is a preliminary report by
. Cairns on the subject. The Legal
ision informs me that a final
ort would be a long project, as
y laws would have to be examined,
they will be glad to undertake it
you wish.

H.D.W.

MR. WHITE
Branch 2058 - Room 214½

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GENERAL COUNSEL
TREASURY DEPARTMENT
WASHINGTON

AUG 31 1942

To: Dr. White

From: Mr. Cairns

On August 29, 1942, you requested that you be furnished with a memorandum setting forth some of the more important powers of the War Production Board or the Chairman thereof, in order that you might form a tentative conclusion on whether those powers were sufficient to enable the Board or its Chairman adequately to supply the materials and equipment necessary for the war program.

In the following discussion, some of the more important powers are listed.

1. The Chairman may exercise "general direction" over the war production and war procurement programs. (Executive Order No. 9024, 7 Fed. Reg. 330.)

2. The Chairman may determine the "policies, plans, procedures, and methods" of any executive department, establishment, or agency with respect to "war procurement and production, including purchasing, contracting, specifications, and construction; and including conversion, requisitioning, plant expansion, and financing thereof". In respect to that authority, the Chairman may issue directives with which the departments, establishments,

FOR DEFENSE
BUY
UNITED STATES SAVINGS BONDS AND STAMPS

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and agencies must comply. Likewise, such departments, establishments, and agencies must furnish such information relating to war procurement and production as the Chairman deems necessary. (Executive Order No. 9024, 7 Fed. Reg. 330.)

3. (a) The Chairman may, through the head of any department of the Government, place an order with any concern for any product or material which is required and which is of a kind produced or capable of being produced by the concern. Such orders are obligatory upon the concern and must be given precedence over all other orders or contracts made prior to the Chairman's order.

(b) If a concern, manufacturing arms, ammunition, or equipment for the Army or Navy, or capable, in the opinion of the Secretary of War or Navy, of being transformed into a concern so manufacturing, refuses to fill such orders or to manufacture the kind, quality, or quantity of such arms, ammunition, equipment, or parts thereof as the Secretary of War or Navy may order, the Chairman, through the head of any department of the Government, is authorized to take possession of the concern's plant and to run it. (Executive Order No. 9040, 7 Fed. Reg. 527, read in connection with section 120 of National Defense Act of 1916, 39 Stat. 213, Executive Order 8629, 6 Fed. Reg. 191, section 9 of Selective Training and Service Act of 1940, 54 Stat. 892.)

4. The Chairman has all the functions, duties, powers, authority, and discretion given to the President by Title III of

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the Second War Powers Act, 1942 (Public Law 507, 77th Congress).

(a) Accordingly, the Chairman may assign and rate priorities for delivery of materials (1) under contracts or orders of the Army or Navy, (2) under lend-lease contracts or orders, (3) under contracts which the Chairman deems necessary or appropriate to promote the defense of the United States, (4) under any subcontract or suborder which the Chairman deems necessary or appropriate to the fulfillment of any of the aforesaid contracts or orders. For the purpose of assuring priority, the Chairman may require acceptance and performance of any contract or order in preference to other contracts and orders.

(b) Furthermore, if he finds that there may be a shortage, the Chairman may allocate any materials and facilities in any manner and under such conditions as he deems necessary.

(c) For the purpose of aiding the administration of his powers under Title III of the Second War Powers Act, 1942, the Chairman may issue subpoenas, obtain information, and require the production of books. (Executive Order No. 9125, 7 Fed. Reg. 2719.)

I must point out, however, that some of the rationing power has been delegated to the Office of Price Administration with the approval or ratification of the President and cannot, therefore, be revoked without his approval. (Directive No. 1, 7 Fed. Reg. 562, Executive Order No. 9125, 7 Fed. Reg. 2719.)

5. The Chairman exercises control over the requisitioning of military and naval equipment or munitions and materials and tools therefor by other agencies and may exercise such requisitioning power himself. He has power over disposal of property requisitioned by

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himself or other agencies. (Executive Order No. 9040, 7 Fed. Reg. 527, read in connection with Executive Order No. 8942, 6 Fed. Reg. 5909.)

6. The Chairman may formulate and execute (using other departments and agencies of the Government to the maximum extent compatible with efficiency) all measures needful and appropriate (1) to increase, accelerate, and regulate the production and supply of materials, articles, and equipment and the provision of plant facilities and services required by the national defense; and (2) to insure effective coordination of those activities of the agencies of the Government concerned therewith. (Executive Order No. 9040, 7 Fed. Reg. 527, and Executive Order No. 8629, 6 Fed. Reg. 191.)

7. Plan and take all lawful steps necessary to assure the provision of an adequate supply of the raw materials required for defense. (Executive Order No. 9040, 7 Fed. Reg. 527, and Executive Order No. 8629, 6 Fed. Reg. 191.)

8. Formulate and take all lawful steps necessary to execute plans for the mobilization for defense of the production facilities of the Nation. (Executive Order No. 9040, 7 Fed. Reg. 527, and Executive Order No. 8629, 6 Fed. Reg. 191.)

9. The Chairman is under a duty and is fully empowered to mobilize aggressively the productive capacity of all small business concerns and to determine the means by which such concerns can be most effectively utilized to augment war production. (Act of June 11, 1942 (Public Law 603, 77th Congress)).

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10. Through his appointment of the directors, the Chairman has control of the Smaller War Plants Corporation. That, with other powers in the Act of June 11, 1942, gives the Chairman power to completely exercise any procurement power that may be vested in any agency or officer of the Government. That results as follows: If the Chairman certifies to any procurement officer (including those of the War, Navy, and Treasury Departments) that the Corporation is competent to perform any specific contract to be let by any such procurement officer, the contract must be let to the Corporation upon such terms and upon such conditions as may be specified by the Chairman. The Corporation then is authorized to arrange for the performance of such contracts by letting subcontracts to small business concerns <u>or others</u> for the manufacture, supply, or assembly of such articles, equipment, supplies, materials, or parts thereof, or servicing or processing in connection therewith, or such management services as may be necessary to enable the Corporation to perform its contract with the United States. (Act of June 11, 1942 (Public Law 603, 77th Congress)).

11. The Chairman is authorized, after consulting with the Attorney General, to permit any person to disregard the anti-trust and Federal Trade Commission laws.

The foregoing are only some of the powers and authority of the Chairman of the War Production Board. If after examining

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this memorandum you feel that it is necessary to continue the search for other powers, I shall be glad to discuss with you the extent and purpose of such a search.

I must point out that much of the foregoing authority may have been delegated by the Chairman to other officers and agencies. Such authority can, of course, be reclaimed by the Chairman except in those cases where authority has been delegated by the Chairman with the approval of the President, for example, the delegation to the Office of Price Administration in Directive No. 1, 7 Fed. Reg. 562, of the rationing authority over sales at retail or to ultimate consumers.

Huntington Cairns
Assistant General Counsel.

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE August 31, 1942.

TO Secretary Morgenthau

FROM Ferdinand Kuhn, Jr.

You asked the other day about Richard K. Law, the son of the late Prime Minister, Bonar Law. He is now serving as Parliamentary Under Secretary for Foreign Affairs, which means that he is Eden's righthand man in the House of Commons, but he will go much farther before he is through. He is one of the ablest and most courageous of the younger political figures in England.

As you will see in the attached biography from the British "Who's Who", he started as a newspaper reporter in this country. He first came into political prominence during the Munich period, when he was one of the Churchill group that attacked Chamberlain. Richard Law not only showed a good grasp of foreign affairs, but he had a kind of bulldog agressiveness about him which Eden and some of the others in his group lacked. He saw clearly what was coming, and he was not too polite towards those who pretended not to see.

When Churchill came into power, Law was appointed Financial Under Secretary to the War Office, and no doubt picked up a good deal of information and experience in military matters.

His constituency is the city of Hull, which has been raided pretty heavily and consistently.

F. K.

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TREASURY DEPARTMENT

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DATE August 31, 1942.

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F. K.

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LAW, Richard Kidston; M.P.(Conservative) S.W. Hull since 1931; Financial Secretary, War Office, since 1940; Member Medical Research Council since 1936; Member Industrial Health Research Board;
b. Helensburgh, 27 Feb. 1901; y.s. of late Rt. Hon. Andrew Bonar Law and Annie Pitcairn Robley; m. 1929, Mary Virginia, y.d. of late A. F. Nellis, Rochester, N. Y.; two s. Educ.: Shrewsbury School; St. John's College, Oxford. Travelled in Asia Minor, India, Canada, United States, and South America; editorial staff, Morning Post, 1927; New York Herald-Tribune, 1928; Philadelphia Public Ledger, 1929. Recreations: sailing, walking. Address: 33 Tedworth Square, Chelsea, S.W.3; Dolloways, Buxted, Sussex. Clubs: Carlton; Constitutional, Hull.

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION CONFIDENTIAL

DATE August 31, 1942

TO Secretary Morgenthau

FROM Mr. Haas

Subject: The Business Situation,
Week ending August 29, 1942.

Summary

(1) Factory employment and payrolls rose to new peak levels in July. Payrolls continued to rise somewhat more rapidly than employment, with the result that estimated average weekly earnings of factory workers showed a further moderate gain. Since July 1940, factory payrolls have increased 106 percent while employment has gained 37 percent. Average weekly earnings of factory workers rose 51 percent during the 2-year period.

(2) Department store sales have been improving recently, although in the week ended August 22 they were still 3 percent under the corresponding period of 1941, when heavy scare buying was in progress. The July decline in department store sales was less than seasonal, and the FRB adjusted index of department store sales consequently shows a sharp upturn in that month. Sales by variety stores and food stores, and even rural retail sales, are running noticeably higher than last year.

(3) Basic commodity prices in the aggregate showed little change last week. However, near the end of the week prices of agricultural commodities, led by cotton and wheat, strengthened on the news that the President's anti-inflation program contemplates flexible rather than rigid stabilization of prices. The BLS all-commodity index of wholesale prices in the week ended August 22 was unchanged at its recent high of 98.9, which is 31.9 percent above the pre-war level of August 1939.

(4) Prices received by farmers in mid-August were 5.8 percent above mid-July, while prices paid for goods bought by farmers were unchanged for the fourth consecutive month. As a result, the index of prices received jumped to a new high at 107 percent of parity, as compared with 101 percent in mid-July.

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Factory employment and payrolls reach new high

Factory employment and payrolls continued to expand in July, and new record high levels were reached, according to preliminary and confidential BLS data. From mid-June to mid-July, factory employment rose 1.8 percent while factory payrolls gained 2.4 percent. Since payrolls continued to rise at a more rapid rate than employment, estimated average weekly earnings of factory workers also showed a further advance to a new high. (See Chart 1.)

Last month rounded out the second full year of marked expansion in factory employment and payrolls growing out of the national defense program and war effort. During that time, employment increased 37 percent while payrolls rose 106 percent. The more rapid increase in payrolls has reflected the longer working hours and higher wage rates in industry since the defense program got under way. As a result, estimated average weekly earning of factory workers in July were 51 percent higher than in July 1940.

Despite the substantial rise already shown in factory workers' earnings during the past 2 years, further gains in wage concessions continue to be made. Thus during the past week, 5 U. S. Steel Corporation subsidiaries were ordered by the WLB to raise the wages of some 250,000 employees 5½ cents per hour retroactively to February 15. The company had previously assented to the wage increase but had contested demands for retroactive payments.

Retail sales improved

The continued rise in employment and payrolls has, no doubt, contributed to reported improvement in retail sales recently, although some expansion is to be expected at this time of the year due to seasonal factors. Department store sales showed their fourth consecutive increases in the week ended August 22, but were still 3 percent under the corresponding week of 1941, due to the heavy volume of scare buying under way at that time. (See Chart 2.) In commenting on last week's trade, Dun and Bradstreet refer to a freer spending mood and an increase in store attendance, with some retailers reporting the largest shopping crowds since early spring.

Variety and food store sales strong

The mid-summer decline in department store sales actually was less than seasonal, and as a result the FRB adjusted index of

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sales for July rose to 117 from 104 in the previous month, thus interrupting the decline that had been in progress since January. (See Chart 3.) Seasonally-adjusted variety store sales and rural sales also improved in July with the former reaching a new peak. Moreover, in both instances the gain over year-earlier levels was noticeably greater than in department store sales. Thus variety store sales were about 17 percent above year-earlier levels and rural retail sales were about 6 percent higher, in contrast with a very narrow gain of only 2 percent in department store sales. This suggests that department store sales should not be too closely relied upon as a measure of current consumer spending.

Seasonally-adjusted sales of food stores in July also moved higher and ran about 22 percent above year-earlier levels, according to confidential Department of Commerce data. Much of this rise, however, was accounted for by the intervening advance in food prices, which amounted to nearly 17 percent.

Some retail sales divisions hard hit

In contrast with the relatively strong showing of variety and food store sales, some branches of retail trade are being hard hit by restrictions and shifts in consumption growing out of war-time conditions. In addition to the heavy dent in total retail sales caused by the restrictions in automotive lines, predictions are now being heard of heavy declines in other lines, such as furniture. Retail furniture business is said to be lagging, and new wholesale business booked by manufacturers in July was reported to be substantially under year-earlier levels.

Although sales of women's clothing are strong, marked buying hesistancy is reported in the men's clothing division, due to the effects of the draft and recent indications of a broadening in classifications liable for Selective Service.

Staple commodity prices rise

Early last week basic prices marked time as commodity markets awaited clarification of the President's new anti-inflation program. Following the President's statement on Friday that the program will involve flexible stabilization of wages and farm prices rather than the anticipated rigid ceilings, agricultural commodities, led by cotton, spurted upward.

The rise was reflected only slightly in the index of 28 basic commodities, since the index of 19 controlled commodities

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remained unchanged. (See Chart 4.) The index of 9 uncontrolled commodities rose to its level of early August, but is still substantially below its peak of mid-May. Cotton and rosin prices advanced to their highest levels since late July.

Wheat, rye, and oats prices increased moderately, while barley, corn, and butter were off. Flaxseed prices rose on the Government's pegging of the flaxseed price at $2.40 a bushel. Prices for steers remained unchanged, while hog prices declined to their level of August 7, influenced by renewed talk of ceilings on livestock.

The BLS all-commodity index in the week ended August 22 remained unchanged at its new high of the previous week. At 98.9, the index stands 31.9 percent above the pre-war level of August 1939.

Farm product prices up sharply to 107 percent of parity

Prices received by farmers as of August 15 increased 5.8 percent from the levels of July 15, and stood 24.4 percent higher than in August 1941, according to the Department of Agriculture's weighted index. (See Chart 5.) Prices paid by farmers, however, remained unchanged for the fourth consecutive month, thus reflecting the stability maintained since issuance of the general maximum price regulation.

As a result, the index of prices received by farmers in mid-August rose to 107 percent of parity from 101 percent in mid-July. This was the sharpest advance since April 1941, even exceeding the increase last December following our entry into the war. All groups except cotton and cottonseed, grain, fruit, and dairy products averaged above parity on August 15, although individual products in other groups remained below parity.

Tobacco, meat animals, truck crops, and dairy products were primarily responsible for the sharp upturn in the index of farm product prices in August. Prices of chickens and eggs also advanced markedly. Grains remained unchanged. Fruits and cotton and cottonseed declined. On a seasonally-adjusted basis all major groups of farm product prices increased, although prices of some individual products declined, among which were apples and potatoes.

The index of farm wage rates, which are not included in the index of prices paid by farmers, increased 10.4 percent as of July 1 from a month earlier, and stood 26.2 percent higher than on July 1, 1941.

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An emergency order "freezing" flue-cured leaf tobacco prices has been issued by the OPA, effective today. The action was taken because price trends indicated "grave danger" of a "run-away market." Prices are about 35 percent higher than those of last season, and are at levels last reached in 1919.

Price floor and ceiling on livestock prices suggested

As livestock producers seem to be losing their fight to keep the Government from placing ceilings on livestock, press reports indicate that a system of price support for livestock as a complementary measure is gaining favor among Agriculture officials and livestock producers. Agitation for such support may be based partly on the belief held in some quarters that the forthcoming record hog crop entering the market this fall may depress prices "to dangerous lows".

Meanwhile, as is shown on Chart 6, the packers' gross margin on pork products continues at the unprofitable level of recent months. According to the press, packers are continuing to bid for hogs despite the shortage in order to keep employees busy, as a shortage of labor is expected as soon as the fall movement of hogs starts to market. Reports are current in the press that confusion over wholesale meat prices, because of ceilings governing innumerable grades, has resulted in penetrations of ceilings and in effect "black selling". Such evasions have taken the same form as evasions in other commodity fields. For instance, meat has been graded to a higher quality than normal by calling "good" meat "choice". In addition, new meat classifications have been created. A third evasion reported is the selling of price-controlled meat only if meat not under price ceilings also is purchased. In these cases the buyer pays an excessive price for the uncontrolled product.

Cotton going into Government loan as withholding movement develops

Even though the cotton loan rate is not high enough to attract much cotton on the basis of current prices, reports from the interior now indicate that substantial quantities of cotton may go into the loan. In addition to cotton farmers' profitable experience with the Government loan in the last two seasons, other factors are encouraging such a development. A cotton-holding movement by Southern farmers is being sponsored by Senators Bankhead, O'Daniel, and Thomas of Oklahoma. In addition, State Agricultural Commissioners are supporting the

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movement throughout the Cotton Belt. Senator Bankhead in a Texas speech urged cotton farmers to put half of this year's crop into the Government loan and keep it off the market until the price has reached near the ceiling level of 21.47 cents a pound.

Despite this withholding movement, and a recent announcement that the Agricultural Marketing Administration may buy in the open market a substantial quantity of cotton of the better grades and longer staples for Lend-Lease distribution, it is felt in some trade circles that cotton prices may decline further under weight of the crop movement now getting under way.

According to press reports, the American Cotton Shippers' Association has issued a report stressing the scarcity of higher grade upland cotton, and urging the Government to reduce Army specifications for certain finished products so as to use lower grades of cotton, which will be in much more plentiful supply.

Canadian price controls jeopardized by weaknesses here

At a press conference last week shared with Price Administrator Henderson, Mr. Donald Gordon, Chairman of the Canadian War-Time Prices and Trade Board, warned that Canada will be unable to hold its price ceilings unless the United States adopts more stringent controls, especially over farm prices and wages. He pointed out that where imports are involved, Canada's subsidy problem has increased. He stated that some $10 million to $12 million has been paid so far to subsidize products imported from the United States at prices above the Canadian ceilings. As an example, he cited beef cattle from the United States, which are selling at $3 to $3.50 above the Canadian ceiling, with the Government making up the difference by a subsidy.

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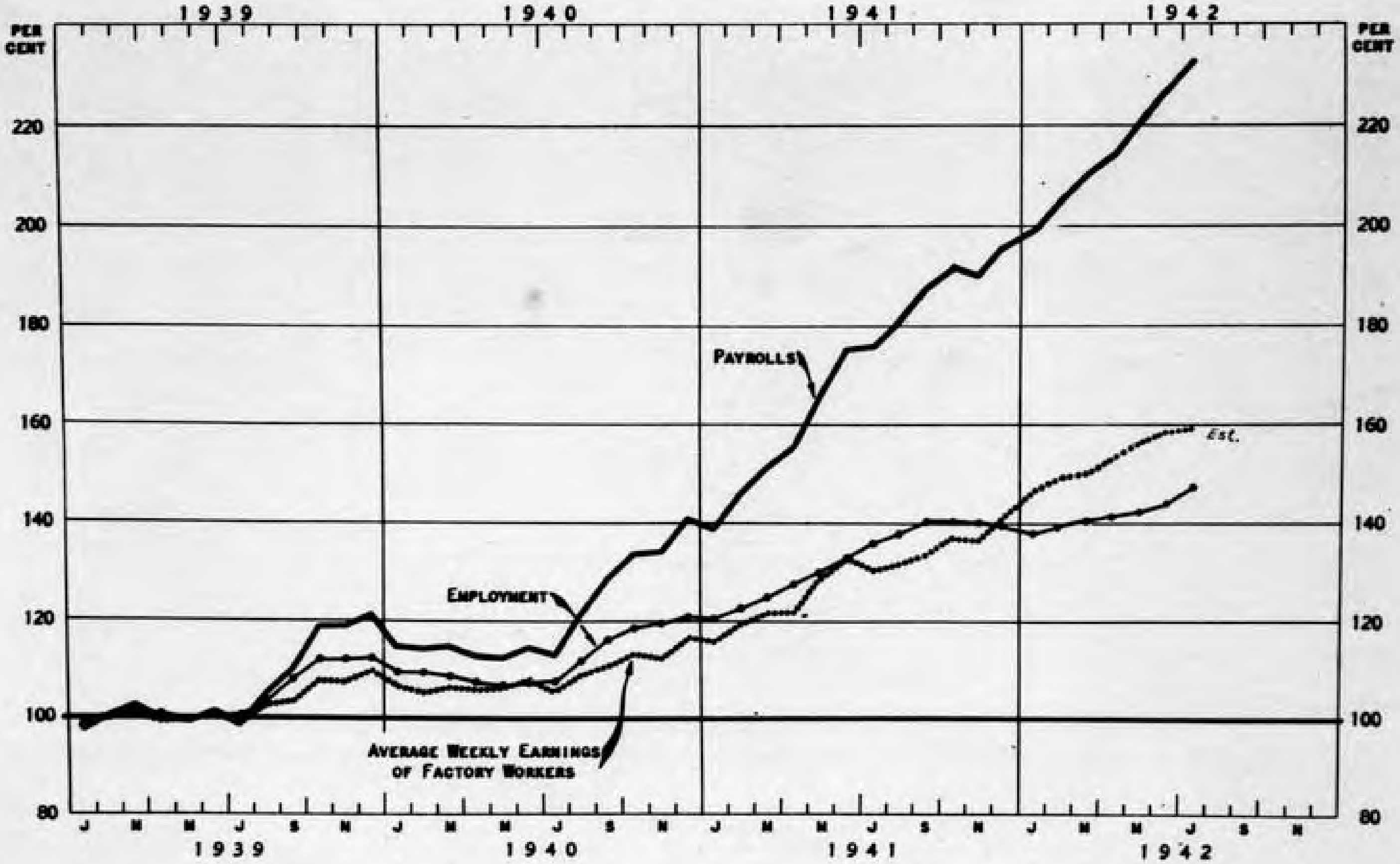
FACTORY EMPLOYMENT, PAYROLLS AND WAGES

First 6 Months of 1939 = 100, Unadjusted



Source: B.L.S.

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

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Chart 1

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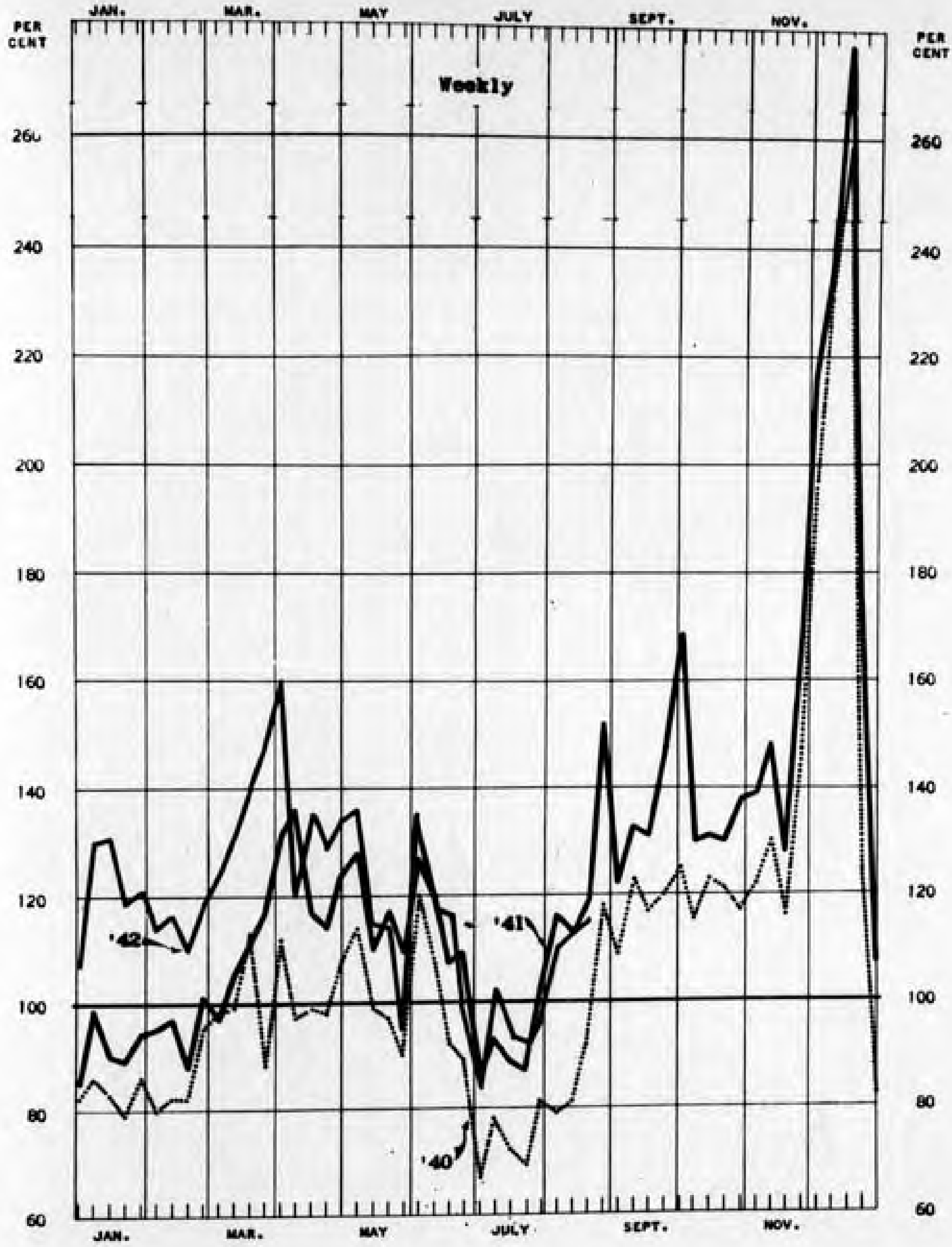
Chart 2

DEPARTMENT STORE SALES

1935 - '39 = 100, UNADJUSTED



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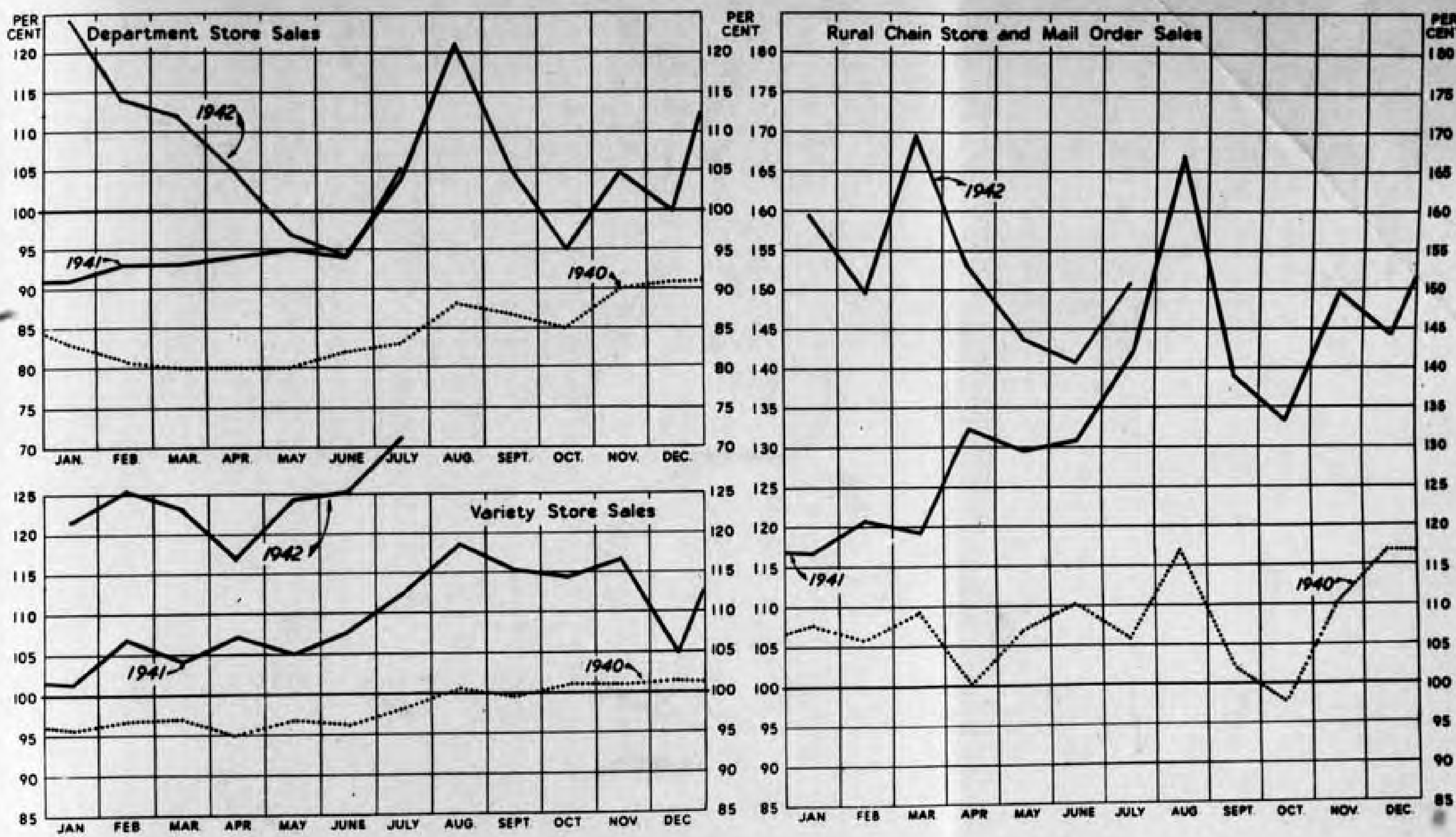
RETAIL TRADE

Urban and Rural Sales of General Merchandise

1929 = 100, ADJUSTED



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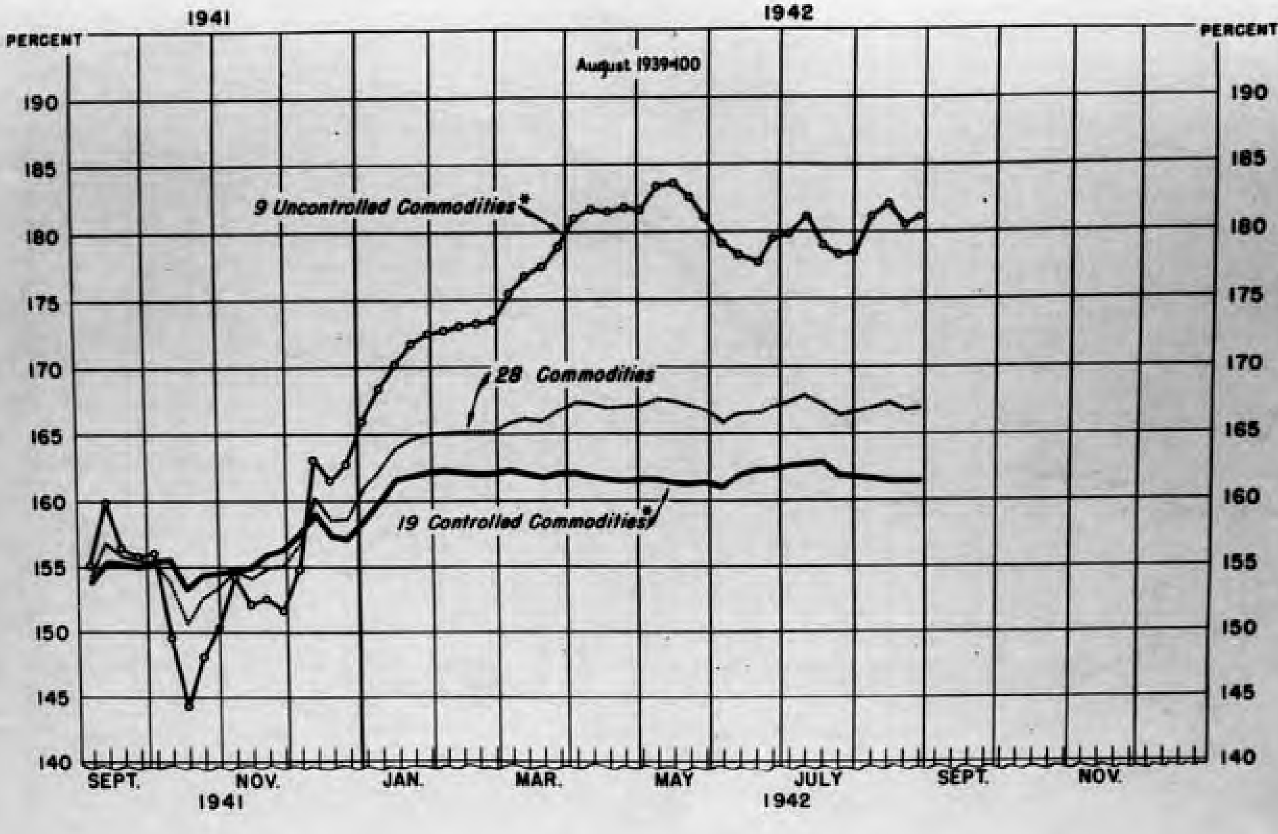
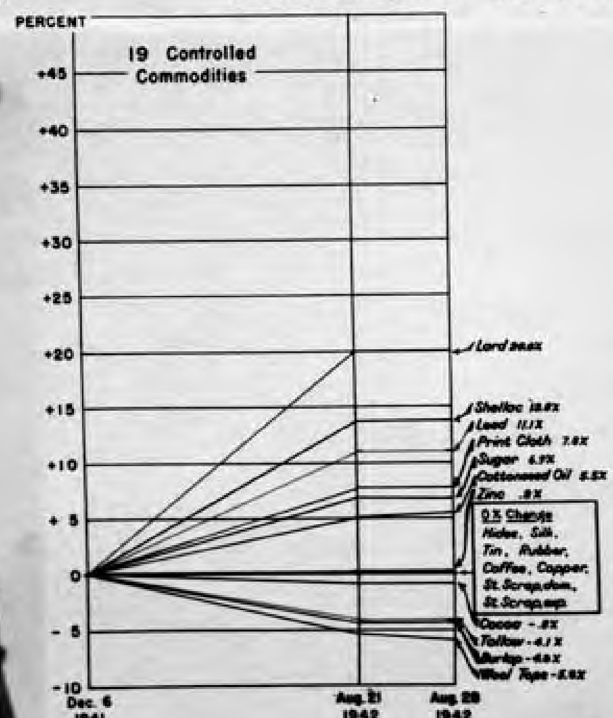
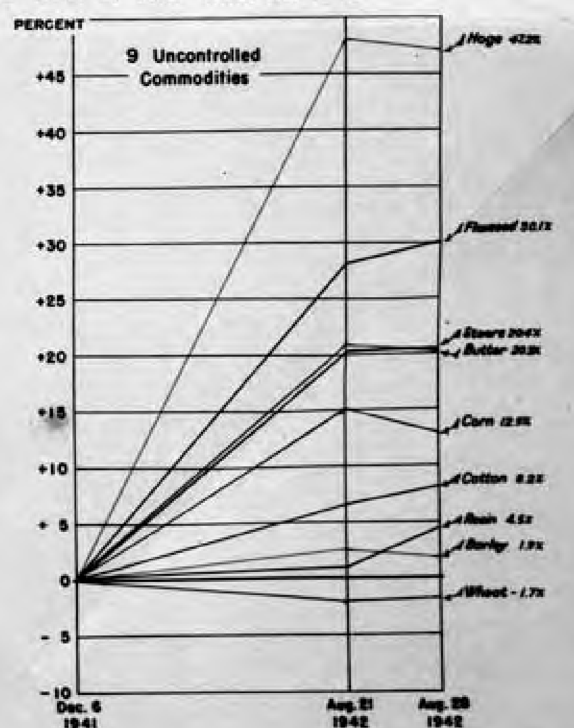
MOVEMENT OF BASIC COMMODITY PRICES



PERCENTAGE CHANGE DEC. 6, 1941 TO AUG. 21 AND AUG. 28, 1942





* 20 Controlled and 8 Uncontrolled previous to June 26

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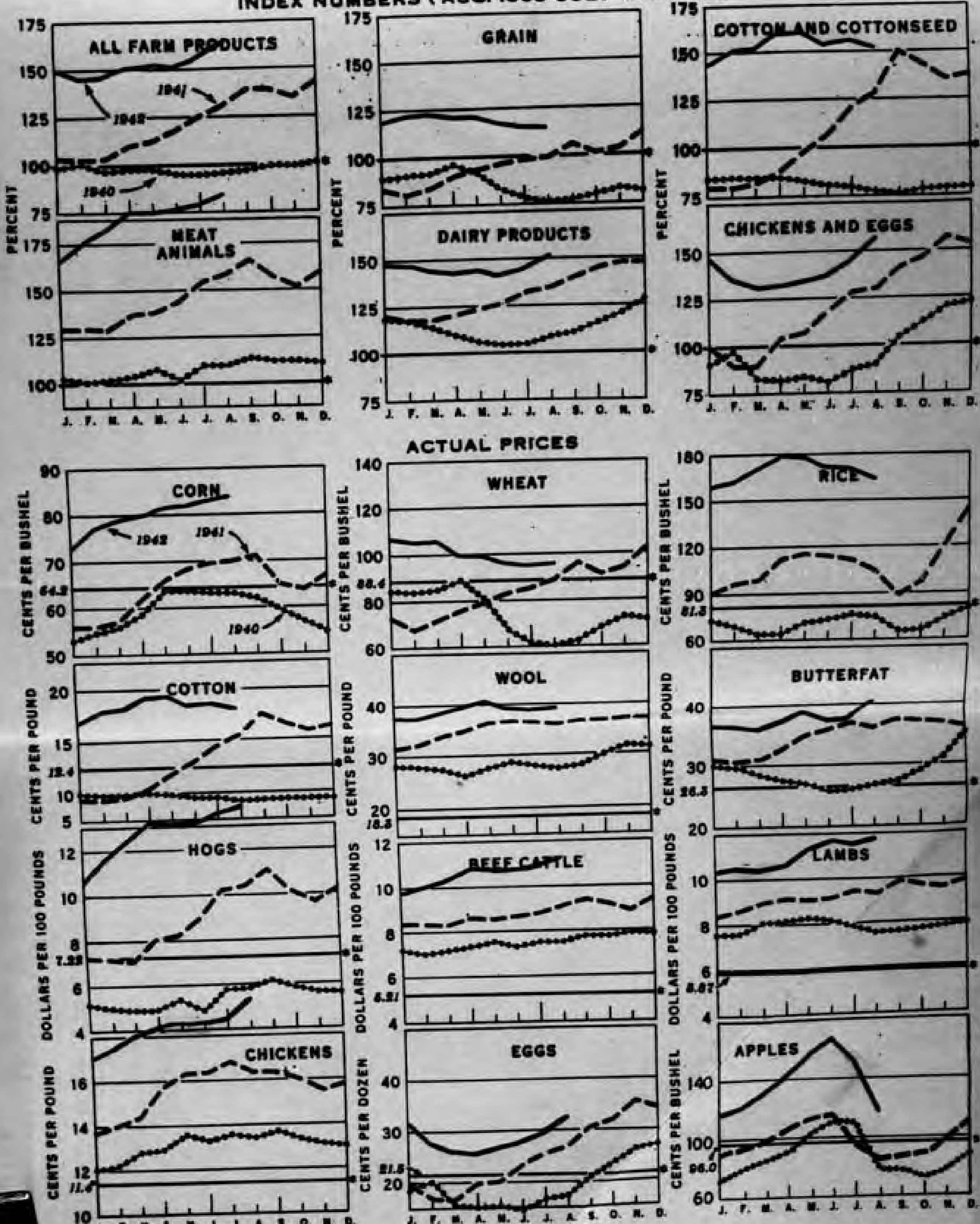
AVERAGE PRICES RECEIVED BY FARMERS: GRAPHIC SUMMARY FOR THE UNITED STATES

INDEX NUMBERS (AUG. 1909-JULY 1914=100)



● 5-YEAR AVERAGE, AUGUST 1909 - JULY 1914

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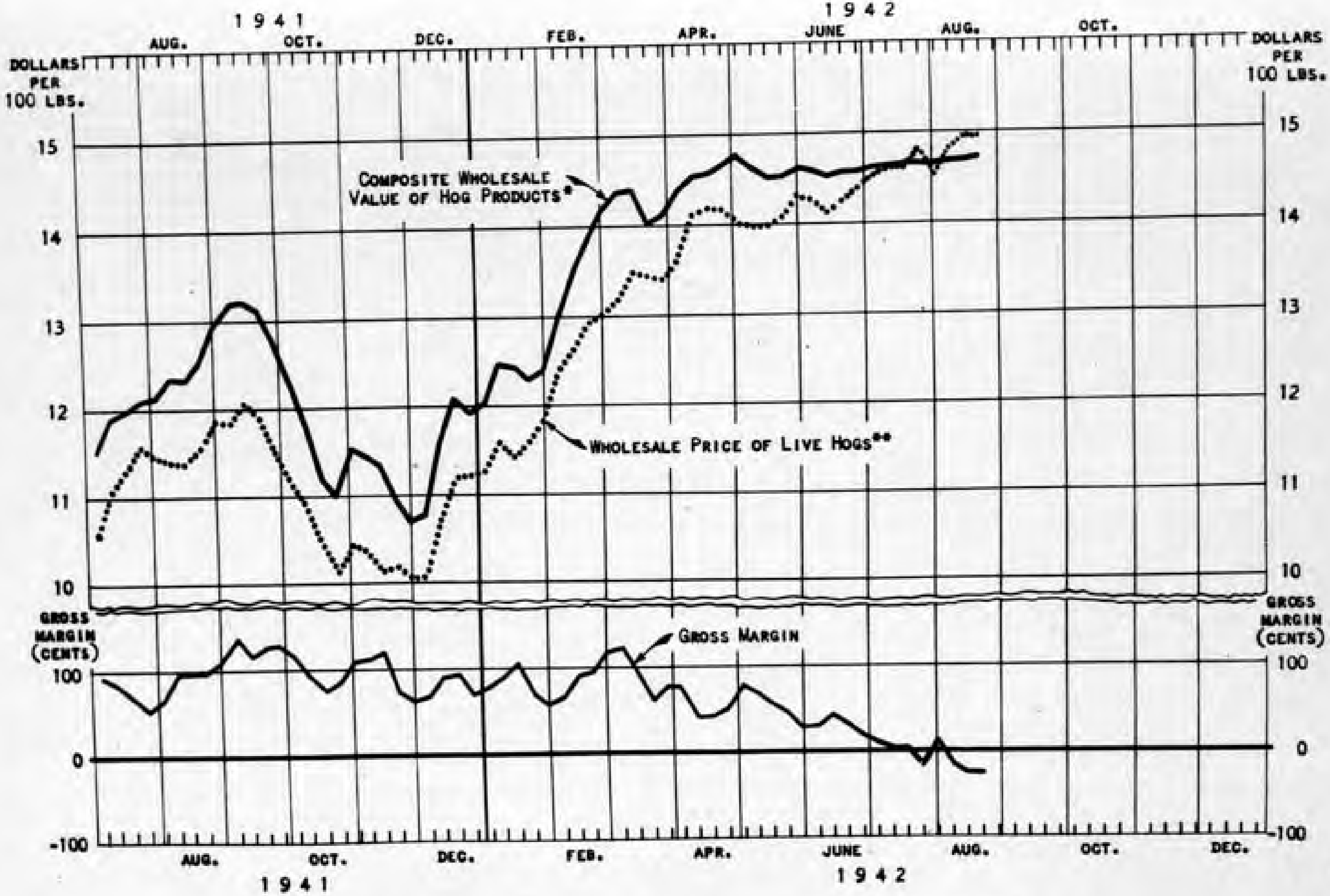
Weekly, July 1941 to date



* WHOLESALE VALUE OF ALL EDIBLE PRODUCTS IN 100 LB. OF LIVE HOGS.
** GOOD CHOICE, 180-200 LBS.

SOURCE: U.S.D.A.

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Division ... Statistics

Chart 6

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BRITISH MOST SECRET
U.S. SECRET

COPY NO. 13

OPTEL No. 297

Information received up to 7 A.M., 31st August, 1942.

1. NAVAL

MEDITERRANEAN. Three of H.M. Destroyers bombarded the EL DABA area early on the 29th starting a large fire. One of them was disabled by an E-boat and was towed into port with 10 casualties. The E-boat was sunk by a naval aircraft, another of the destroyers was slightly damaged by air attack.

2. AIR OPERATIONS

WESTERN FRONT. 29th. A section of Spitfires flying at 40,600 feet over Southwest ENGLAND sighted, but were unable to engage an enemy aircraft, believed a JU 86 which was 900 feet above them.

30th to 31st. Nothing of importance to report.

EGYPT. 28th to 29th. Our bombers again attacked TOBRUK Harbour hitting two ships. The railway and landing ground at EL DABA and M.T. in the battle area were also attacked. Enemy bombers operated in the ALEXANDRIA area mainly against landing grounds and caused some damage to grounded aircraft. One was shot down.

29th. Our fighters patrolling over a naval unit shot down three fighters and probably destroyed three more. Another was destroyed by A.A. fire. We lost two fighters.

OPTEL No. 298

EGYPT. In early hours of 31st enemy attacked on southern sector of EL ALAMEIN position. Enemy moved forward in 2 main columns between QARET EL KHADIM and QUARET EL HEMEIMAT. Northern column estimated 140 tanks and southern column 70 tanks and 500 M.T., tanks mostly German. No further details available. Nothing to report from northern sector.

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NOT TO BE RE-TRANSMITTED

COPY NO. 13

BRITISH MOST SECRET
U.S. SECRET

OPTEL No. 301

EGYPT. Night 31st/1st troops of 9th Australian Division in northern sector made successful raid taking one hundred German prisoners. Enemy concentrations heavily bombed by R.A.F. with great success.

1st. Enemy columns on our southern flank, which had pushed forward on 31st, swung northwards towards central sector of our front. In spite of repeated armoured attacks, they have made progress only by skirting our strong points and concentrations and have been held wherever they have made direct attacks. Th head of main enemy column has reached ALEM EL BUEIB about 9 miles S.S.W. of EL IMAYID, while the tail is being attacked by our troops from the south.

OPTEL No. 302

Information received up to 7 A.M., 2nd September, 1942.

1. NAVAL

A Dutch motor fishing vessel which surrendered on 31st to one of H.M. trawlers has arrived at HARTLEPOOL.

2. MILITARY

RUSSIA. German forces are making some slight progress towards STALINGRAD from the south-west. In the western CAUCASUS, Russian resistance has held up German progress but the Germans claim the capture of ANAPA on the Black Sea Coast.

3. AIR OPERATIONS

WESTERN FRONT. 1st. Offensive patrols which were uneventful included sorties by 32 U.S. Lightnings. One Spitfire did not return. 1st/2nd. 231 aircraft were sent to SAARBRUCKEN. First reports from all groups indicate a highly successful attack in excellent weather, fires were large and well concentrated, 4 bombers are missing and 2 crashed.

EGYPT. 30th/31st. Enemy aircraft attacked our landing grounds south of ALEXANDRIA, night fighters destroyed 2 and A.A. probably destroyed another.

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31st. Dust storms restricted our operations, but escorted light bombers successfully attacked enemy concentrations in the southern sector and road traffic near SIDI BARRANI. Our fighters intercepted 2 escorted dive bomber formations, one of which was forced to jettison its bombs. Fighters destroyed 7 enemy aircraft including 2 JU. 52's and 3 dive bombers and A.A. shot down 8 more in the forward area. 3 of our fighters are missing.

4. HOME SECURITY

1st/2nd. Some bombs dropped at DONCASTER caused damage to premises in the shopping centre and slightly affected utility services. There were also some casualties.

Regraded Unclassified

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE August 31, 1942

TO Secretary Morgenthau

FROM Ferdinand Kuhn, Jr.

You may be interested in the following excerpt from the British Ministry of Information's "Home Intelligence Report" for the week ending August 17th:

> "In a number of regions appreciation of U. S. troops in Great Britain is reported. Troops are described as 'singularly good fellows,' setting an example for other visitors. In regions where troops are stationed, residents are anxious to be hospitable and are devising entertainment for them. In northwestern and southwest regions adverse comment is reported regarding colored troops, arising over girls who 'walk out with them.' The criticism is directed at the girls rather than at the troops themselves. As a solution the introduction of colored women auxiliaries is widely advocated as it is felt that 'repressive measures' are unsatisfactory with 'certain types of girls.' At the same time the extremely pleasing manners of the colored troops are remarked. In three regions there are references to drunkenness among U. S. troops. Complaints of alleged excessive charges by shopkeepers in Northern Ireland have recently been investigated. The only specific complaints found concerned coffee and whisky prices."

F. K.

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