

The world monetary crisis turns against the U.S.

by David Goldman

Federal Reserve Chairman Paul Volcker, reappointed by President Reagan in July, postponed a general crisis of the banking system until early 1984, but at the expense of putting the United States in line as principal victim of the crisis when it emerges. The theme of the October meeting of the International Monetary Fund, echoed in IMF and European government statements since, is that the American budget deficit—implicitly, the President's defense program—is the central cause of the present world monetary crisis. In fact, the end-product of Paul Volcker's financial regime of the past year, which has made the U.S. Treasury the sinkhole for international flows of flight capital, will make the Treasury the major casualty when a banking crisis interrupts such flows.

At the end of 1982, Treasury Secretary Donald Regan and Fed Chairman Paul Volcker, with the support of Secretary of State George Shultz, determined to crush the growing initiative for joint debt moratoria on the part of the major Ibero-American debtors—as proposed by former Mexican President José López Portillo to his Argentine and Brazilian colleagues in October 1982. The American monetary leadership adopted a policy which might politely be characterized as fraud and blackmail to avert this. The fraud consisted in first the allegation, and then the outright manufacture of statistics (as exposed by *EIR* in an autumn 1983 investigation) pertaining to "American economic recovery." No recovery ever existed, merely a deceleration from the 1982 rate of decline brought about by \$100 billion of federal "off-budget"

support for the housing and other consumer sectors. The blackmail consisted in threats of economic warfare and worse, should countries refuse to cooperate with the International Monetary Fund.

By any normal accounting standard, the major American banks were finished as of March 31, when the major Ibero-American debtors were unable to pay about \$40 billion of interbank lines extended to them the previous fall, in order to "bridge" debt payments coming due which went unpaid then. Brazil was able to pay neither the banks, nor the Bank for International Settlements-led consortium of governments and central banks who had lent the country more than \$2 billion to bridge expected payments from the International Monetary Fund.

Volcker pumped reserves into the banking system throughout the first half of the year at an unprecedented 12 percent annual rate, and ignored the arrears building up on the American money-center banks' accounts—\$3 billion in defaulted interest payments due from Brazil alone by the end of the year.

By mid-July, the proverbial eyeball-to-eyeball confrontation had arrived; the Bank for International Settlements, under the direction of Swiss National Bank chairman Fritz Leutwiler, had not received \$500 million in bridge-loan repayments due the previous month, and threatened to call Brazil into default, a form of financial excommunication which would have triggered an immediate crisis. Volcker's own reappointment was under review by a hostile Reagan

administration which, from its own limited perspective, recognized the Fed chairman as a Carter appointee who meant the White House ill.

Both the Reagan White House and the Ibero-American governments—who could simply have struck a political deal for long-term debt restructuring and averted the crisis—collapsed in front of the terrors presented to them. The major money-center banks, *EIR* revealed, went to the President behind Treasury Secretary Regan and warned that the “recovery” would collapse unless the President turned matters over to them. Meanwhile, they exercised enough of what is politely called influence in the U.S. Senate to credibly tell the White House that no other candidate for Fed chairman but Volcker would be confirmed.

Although the President had entertained early doubts concerning the reports of recovery, the barrage of lies produced in the Federal Reserve basement permitted his “political advisers” to convince him that the recovery was the key to his 1984 political fortunes. The bankers’ blackmail stuck, and Volcker was reappointed. The backdown by the White House permitted the American Treasury to threaten the Brazilians with a cutoff of their oil supplies, and, with oil stocks at two weeks, the Brazilians chose to crumble. A notice of surrender was delivered to the International Monetary Fund, and Brazil ultimately capitulated fully to the IMF in November.

On the surface, the spit-and-chewing-gum methods used to postpone the crisis have become flimsy to the point of absurdity. By Dec. 31, 1983, the major American banks will (as of *EIR*’s deadline) have brought Brazil up to date to Oct. 4, 1983, leaving themselves only 88 days in arrears—or two days away from bankruptcy. If the banks had to close their books Dec. 31 showing billions of dollars of bad Brazilian paper more than 90 days in arrears, U.S. bank regulators would have no choice but to force them to write off most of their Brazilian loans.

The nine top American banks—Chase Manhattan, Citibank, et al.—have between two and three times their shareholders’ capital in Brazilian debt—which is to say that a Brazilian write-off would bankrupt them two or three times over. The only consequence of this exercise in creative bookkeeping will be to postpone the big blowout until March 31, when the banks have to close their books for the next quarter. By this time, the supposed bankers’ rescue package for Brazil will have fallen apart, according to an authoritative, but confidential, U.S. government study.

In October, Lyndon LaRouche issued a statement beginning, “Before Christmas 1983, it is probable that Brazil and other leading nations of Ibero-America will be forced to default officially on their foreign debts.” The present state of affairs in Ibero-America shows that if the bankers have been able to forestall that probability, it has only been by resorting to the kind of fantastic “creative accounting” practices that would send any ordinary bookkeeper to jail.

As *EIR* reported the view of a senior official of the Swiss National Bank, “The debt reschedulings of 1982 were difficult, the second round during 1983 was next to impossible, and the third round in 1984 will fall apart.”

America’s turn in the barrel

Volcker’s grand success of 1983 was to back up the \$800 billion in hopelessly defaulted Third World debt by undermining approximately \$10 trillion of debt in the OECD countries. The dollar’s strength throughout 1983, especially since November, is less a reflection of “confidence” in the American economy than a slow-motion bankruptcy of Western Europe, whose financial system is collapsing under the weight of \$400 billion in net external debt.

And America’s creditor relationship to the rest of the world was maintained at the expense of bankrupting the majority of debtors. In our Year-End Review for 1982, we reported that the developing-sector debt crisis was not the result of overborrowing and overspending by developing countries, but of the reduction of these countries’ terms of trade by half since 1979. The flood of capital inflow into the United States—matched by uncontrollably growing indebtedness on the part of the weaker Western European nations—got the Volcker regime through 1983, by ruining America’s major debtors. Since these debtors are also America’s principal military allies, the implications for America’s world role are deadly.

When Paul Volcker flew home from the October 1979 Belgrade IMF annual meeting in the midst of a crisis that reduced the dollar’s parity to DM 1.78, he “saved” the dollar by imposing a regime of flight capital that brought in \$100 billion from Ibero-America by 1982—bankrupting the continent in the process. With a trade deficit at over \$100 billion, a budget deficit close to \$300 billion (including the buried “off-budget items”), and a current account deficit at almost \$50 billion, the Volcker policy now requires the exhaustion of Europe’s capital resources to finance the external deficits.

Europe is on the line because Ibero-America has been bled dry, and because the OPEC surplus, with some help from Soviet oil-dumping in Europe, has turned into a \$30 to \$40 billion per year deficit. That is, the flood of monetary resources available to the United States as of 1980, when the OPEC surplus totaled \$110 billion per year and the then-prosperous nations of Ibero-America were capable of exporting up to \$40 billion of flight capital per year, is virtually exhausted.

The result of the process is that, despite the phony claims of recovery in America supported only by fraudulent statistics offered by the Federal Reserve, world trade continued to decline throughout 1983.

The flows of wealth, both in the form of the OPEC surplus and the looting of Ibero-American resources (through export of capital, currency devaluations, lowered terms of trade,

rock-bottom commodity prices, and so forth) which supported Paul Volcker's world regime of usury have, inevitably, been consumed. Most of Ibero-America's debt accumulation since 1979, in particular the spectacular rise of interbank borrowings (to a total of \$40 billion) during 1982, represented financing of flight capital and other forms of looting. Western Europe has replaced Ibero-America as the leading source of flight capital, and Western Europe has "sovereign" external debts of over \$300 billion and short-term bank external debts of over \$100 billion.

At what point will the crisis break out? "If you look at the trade and current account deficits, they will be increasing on out as far as the eye can see. The economics of it are inexorable. But as for what will trigger the actual turnaround in the market, this will be a non-economic event," said a leading economic spokesman for the Carrington group in London in a Christmastime chat. "I am thinking of something like, hypothetically, if the President were to announce tomorrow that he wouldn't run for re-election. If no adverse political development occurs, the dollar can remain on a plateau for some time, or bump further upwards. But the history of these things shows that something else always happens—an oil crisis, an assassination, a war, or something like that. What is tricky in this case is that the dollar is a haven currency, and some developments like this would be good for the U.S., and lead to a stronger dollar in the short term. So it has to be something damaging to the United States, raising questions about U.S. economic policy."

Asked what this implies for the American budget deficit, Carrington's associate said, "This is what is poorly understood. For this year, by most estimates for current account—although the discrepancy [the errors and omissions] make this a bit difficult—show foreign capital inflow of about 1 percent of GNP, with a deficit at about 5 percent of GNP. All forecasts for next year show the inflow at about 1 to 2 percent of GNP. But that isn't the real problem. When foreigners want to go out, they can't, not until the current account turns around. But even if they can't get out, they will try to get out, which creates the potential for a very big and very sudden drop in the exchange rate. *The sudden desire of people to get out of the dollar will push up U.S. interest rates.* If this is triggered by a dramatic non-economic event, the slipover from the present situation to one in which everyone will try to get out will be enormous."

That is what the defense-budget-cutting cabal—from Helmut Schmidt to Margaret Thatcher, from Robert Dole to Tip O'Neill—expects to "de-fang Reagan," to quote the phrase of a Soviet economist. The financial mess is supposed to play into a general backdown on the part of the Reagan administration, permitting the decoupling of Europe from NATO and the crumbling of the Mideast.

The end of governments

The end-product of the slaughter is described with un-

usual frankness by the International Monetary Fund in an appendix to its 1983 *World Economic Outlook*: The IMF reports that funds equal to about a quarter of world trade now cross national borders untracked by governments. As *EIR* has exposed in detail, this includes flight capital, narcotics revenues, illegal arms, smuggled gold, contraband high-value agricultural products like coffee, and human beings, and it represents a \$300 to \$400 billion per year flow of funds, the margin of available cash in the world economy. This is the pool of international funds the United States is now drawing on to finance its external and internal payments deficits, and that defines an American weakness.

The \$300 to \$400 billion a year flow of untraceable money corresponds to hidden trust assets which, as *EIR* first reported in 1981, control roughly \$200 billion of American equity unregistered with U. S. authorities, as well as substantial portions of the "visible economy." It also represents a Soviet strategic capability. The British, Swiss, Hong Kong, Singapore, and other investment and commercial banks who provide the "shells" through which such funds are invested untraceably are the Soviets' partners in what is euphemistically known as the "underground economy."

From the center of an international network that controls a large part of world narcotics traffic, gold smuggling, weapons contraband, and similar activities, the Soviets operate one of the largest of the world's major *fondi* (concentrated, usually family-based, investment holdings). Available indications are that the Soviet *fondo* represents a joint venture with British and Swiss partners, of which the leading Western figure is the new Secretary-General of NATO, Britain's Lord Carrington. At the point of takeoff of Soviet Empire financial operations, Moscow Narodny Bank, the Soviet-owned bank in London, formed a joint venture, East-West Trading Ltd., with Carrington's merchant bank, Morgan Grenfell.

One indication of the scope of Soviet operations is the size of foreign-exchange operations conducted in November and December, reported in *EIR*. Moscow Narodny and its sister institutions have accumulated foreign exchange lines of \$100 billion—net of lines available for other purposes—and are capable of operating in all major U.S., European, and Asian money markets simultaneously.

When the United States removed the dollar from gold backing in 1971, it lost control of dollar-based banking operations to the Eurodollar market. When Volcker crushed the debtor nations of the developing sector during 1983, he unleashed a financial whirlwind which has ruined the state finances of Ibero-America and Europe, and now threatens to ruin the United States Treasury. The American banking system is now sitting on a scaffolding controlled, in large measure, by Soviet foreign intelligence operations. The "success" of the Volcker-IMF policy in 1983 will mean America's military, as well as financial, ruin in 1984. The time to consider the consequences of continuing in this direction is now measured in weeks.