

Foreign Exchange by Montresor

This column to be discontinued

Thanks to a run out of all currencies, there soon will be no such thing as foreign exchange.

A comparison of the respective behavior of bond markets in all currencies, and commodity prices in all currencies, makes clear that the underlying impulse of the present crisis, leads toward a run out of all national currencies.

The condition of world trade makes that less than surprising; while world trade as a whole remains below 1980 levels, if we deduct the cancerous increase in American imports, these American imports, as a percentage of world trade, have increased drastically.

In other words, the Third World debt crisis has wiped out what had been, and should have remained, the engine of expansion of international trade; and the subsidy of the failing United States economy, has become the principal source of apparent trade growth for most of America's trading partners.

Correspondingly, the export of American IOUs has turned the Japanese banks into the principal financiers in the dollar sector itself, and increased the dollar's relative proportion of international currency reserves.

Since both the physical trade, and the private and public financial reserves of America's trading partners, depend on the dollar, the collapse of the dollar becomes a collapse of all currencies.

The most vulnerable, because least liquid, sector, is the Eurobond market, whose \$200 billion annual volume compares to less than a tenth that much at the beginning of the decade.

A commentary in the London *Financial Times* of Sept. 14 expressed fears of a general shakeout in Eurobonds, noting, "While the U.S. Treasury can issue its paper come hell or high water, because U.S. primary dealers undertake to underwrite all new Treasury bonds, there is no such commitment from dealers to the issuers in the Eurobond market."

The Sept. 11 report of America's \$16.5 billion July trade deficit "aimed a kick for a market already on its knees. . . . Bond yields in most major currencies seemed to be on an inexorable path upward while a complete absence of investor interest meant that last week's was about the smallest crop of new issues seen in the Eurobond market this year," the *Financial Times* reported.

"In happier times, worries about a sliding dollar would have prompted a rally in D-Mark and Japanese yen bond prices because of prospects for currency appreciation. When the dollar drops these days, so does the U.S. Treasury bond market and its Japanese and German counterparts. 'The worry is that we are seeing a cyclical rise in world interest rates and it's difficult to see what's going to break that cycle,' said a syndicate official at a U.S. firm."

The term, "cyclical rise in interest rates," means nothing; the issue is simply that the long-term profitability of all the major nations' economies is in jeopardy.

There is no other way to explain the generalized rise in commodity prices during the past year. Prior to January 1987, raw materials prices

hovered at about 30% below their 1980 levels, reflecting a deflationary spiral comparable to that of the 1930s.

That was before central banks began the biggest exercise in money-creation in world history, creating \$78 billion of their own currencies during the first half of 1987, in order to purchase unwanted dollars off the floor of the foreign-exchange market.

Many industrial commodities, e.g., silver, lead, cotton, rubber, nickel, wool, copper, aluminum, and other metals, are up 25-50% this year so far, and oil prices have doubled from the lows of a year ago. The London *Economist's* commodity price index has risen 35.6% during the past 12 months.

The Commodity Research Bureau's spot index of raw industrial materials is up 38% over the past year.

Notably, the *Economist's* mixed-currency commodity index has risen 25.8% in the past year. That indicates that the collapse of the dollar (the currency in which most commodities are traded) has had only a limited impact on the rise in commodity prices; most of the rise occurred independent of the dollar's fall against other currencies, which is to say, that the value of commodities rose against all currencies.

Given that there is no industrial demand anywhere in the world, the startling rise of industrial commodities reflects a speculative build-up of inventories of hard, tradeable goods, as a hedge against all currencies. Normally, gold, whose price has risen sharply during the past year, plays this role, along with gold-equivalents such as silver; the system-threatening feature of this development, is that the entire range of durable, fungible commodities has become an inflation-hedge.

That is what makes hyperinflation possible.