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Debt Plunges Western Europe Into New Trade Collapse

Since the first quarter of 1977, the economies of Western Europe have entered a new phase of the depression that promises to dwarf even the 1974-75 production collapse. Despite Carter Administration efforts to force West Germany and Japan to reflate, domestic pump-priming is useless — if not wildly inflationary — in the face of a depression caused by the international debt crisis and the resulting drop-off in advanced sector exports.

In the West German Federal Republic (BRD), the government's industrial order index peaked at 178.6 in March, then plunged 15 percent to only 151.8 in June.

BUSINESS OUTLOOK

BRD industrial output in June was down two and one-half percent from the March level, and represented a mere 1 percent over June 1976. Unemployment has persisted at the 1 million person level all year, despite the original government target of 850,000. In France, production has stagnated since the final quarter of 1976, while unemployment has soared to over 1.2 million in August — the highest level since World War II. In Britain, where unemployment is also at a post-war peak of 1.4 million, industrial production fell 3.7 percent between May and June alone — from an index figure of 104.6 to 100.7, or barely above 1970 levels. In Italy, industrial output fell nearly 3 percent between March and May, and more than 1.4 million persons are out of work.

Both the West German and French governments have recently introduced "anti-depression" pump-priming programs, injecting an additional 24 billion deutschemarks ($10.4 billion) and 8.9 billion francs ($1.8 billion) into their respective economies. Similar measures are under debate in Britain. French Prime Minister Barre has budgeted the first *planned* government deficit in years, amounting to a 12.5 percent increase in overall spending.

The 1978 French budget is a "mixed bag" of tax concessions for lower-income groups, investment incentives for small firms and individuals, and modest hikes in public investment (plus 16.6 percent) and military (plus 16.5 percent) programs. The West German "stimulus" package similarly breaks down into 7.4 billion deutschemarks in tax cuts and a 10.1 percent (17.3 billion deutschemark) increase in government spending. West Germany's program, however, has nothing to do with the Carter Administration's "recovery' program, except in the sense of political kowtowing. This is broadly recognized at the Brookings Institution and other boosters of the "triple reflation" idea. What the West Germans are concerned about is keeping their domestic capital markets on an even keel, and are willing to loosen the money markets to compensate for the end of the inflows of speculative funds. The Federal government and states have a 47 billion DM borrowing requirement this year, according to the most recent official estimates. Virtually none of the so-called stimulus package will affect the real economy.

The actual cause of the depression crisis is the crippling build-up of international debts — including approximately $250 billion owed by non-oil producing Third World countries, $50 billion by the East bloc socialist nations, and $100 billion by Western Europe itself — and the severe "adjustment" by programs which the International Monetary Fund (IMF) has imposed. Although a speculation-induced run-up in world commodity prices of about 15 percent, immediately following Jimmy Carter's election, temporarily propped up the Third World sector allowing most of these countries to meet their heavy first half of 1977 debt service schedules, this "tax" on the advanced sector's industry and population could not be sustained. By April, declining industrial orders and mounting inventories of unsold goods forced the advanced sector to curtail its orders for Third World primary products. Commodity prices promptly fell 25 percent, necessitating a further curtailment of Third World purchases of capital goods needed for development — the depression was on.

Debt Hits BRD Exports

Although West Germany's economy is ideally situated to be the capital goods supplier for the world, the nominal value of BRD exports has actually steadily declined since September-October 1976, with only a slight upward blip in March-April 1977. As the table shows, exports to the socialist and Third World sectors and to the BRD's major EEC trading partners were hardest hit. A country-by-country analysis, however, reveals the true extent of the disaster. BRD exports to the Soviet Union during the first half of the year plunged 12.5 percent from last year's level, as the failure to develop a transfer ruble-based credit system took its toll. West German exports to Denmark fell 8.5 percent from a year ago; the rise of 2.1 and 3.1 percent to France and Italy, is really a decline when inflation is considered. Although West Germany properly ought to be running a gigantic trade *surplus* with the Third World, to achieve the level of capital goods input necessary for industrializing this sector, it actually ran 2.2 billion DM *deficit* with non-European, non-OPEC less-developed countries during the first half of 1977.

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A one-shot order related to the West German-Brazil nuclear deal indicates what could have happened. The BRD government's index of foreign capital goods orders hit 379.6 in July 1976 — nearly four times the 1970 base level. The index never regained that level and was down to 197.3 as of June 1977.

West German corporate profits have already shrunk, due to the production drop and the necessity of keeping prices down to remain competitive under conditions of a rising deutschemark. According to a Reynolds Securities report, the drifting West German stockmarket "reflects increasing disquiet about the trend of profits. In previous reports, we estimated that these rose by 20 percent in 1976 and that they would probably rise by some 8 percent or so in 1977, but this latter estimate must now be reduced to somewhere in the region of zero to plus 5 percent, averaging 2.5 percent."

Rather than investing in new plant and equipment, BRD corporations have been purchasing fixed-interest BRD government securities instead. The "excess liquidity" conditions have resulted in the lowest federal government bond rates since 1964, but this bond market "boom" only covers over the contraction in productive economic activity.

France: "Hard" Franc Policy Guts Consumption

In France, the Barre plan, a domestic austerity program to maintain a stable franc and reduce inflation, has "succeeded" in touching off a 5.8 percent drop in domestic demand. The internal consumption cuts, combined with sluggish export markets, have already produced an upward surge of inventories and production cutbacks. French industrialists, however, have few illusions that Barre's new stimulus plan will have any effect. "Much is made of internal economic problems such as unemployment," stated a spokesman for Usinor, France's steel giant, "but those problems could be quickly solved. The main difficulty is the slowdown of other key world economies. Without a pickup outside France we can't begin to solve our problems."

Although the French trade deficit has gradually narrowed since the third quarter of 1976, this has merely tended to reflect decreased economic activity. In July, both imports and exports fell by 7 percent and 1.5 percent respectively.

The world's financial press stupidly gloats that insolvent Italy is "recovering" since the country ran a trade surplus for two months-running, including a $322.5 million surplus in July. In reality, a sharp production decline has allowed the country to reduce imports of raw materials. The production cutbacks would have been even deeper if it were not for the fact that Italian banks have accumulated a short-term foreign indebtedness of $7.9 billion.

According to a recent survey taken by the Turin Industrialist's Union, representing mainly small businesses, 40 percent of Turin businesses expect a drop in orders and only 15 percent predict increases. Meanwhile, whole chunks of Italy's public sector industry have gone bankrupt and are being placed on the auction block for sale to Lazard Frères-associated banking networks. The government steel and metals company (EGAM) was recently liquidated and the giant holding company (IRI) has requested a $1.3 billion group bailout.

In August, Britain recorded its first trade surplus since 1972 and its largest since July 1970 ($551 million). Although this news was the cause of more speculative euphoria on the British stock market — taking the *Financial Times* 30-stock index beyond its previous May 1972 peak — the sad truth is that imports plunged 12 percent while exports dropped slightly, hardly a sign of industrial recovery. Britain's industrial production index is now precisely where it was seven years ago.

—Alice Roth

Flow Of Third World Loans Go To Debt Payment As Economic Crises Worsens

BANKING

Contrary to statements made by West German, Japanese, and U.S. bankers at the Bank of America-organized Tokyo conference of the American Bankers Association last May, the new series of significant loans granted now to leading Third World countries such as Mexico, the Ivory Coast, and Brazil do not follow a coherent strategy for industrial investment. The loans are being deliberately made to permit further debt repayment. This intervention of international banks, which reverses the pattern of an LDC decrease in borrowing during the first half of 1977, is not a response to the urgent needs of the Third World. Instead bankers are seeking a way to increase their volume of operations so as to artificially compensate for their half dead lending markets in the advanced sector, dried up by the lack of capital formation.

The fact that most of the loans are nominally tied to development projects does not hide the actual debt repayment which is to proceed.

First, all available national resources are now allocated by the planning agencies of the Third World countries to debt repayment. Investments eventually generated by project loans, if any, are not used to create further productive capacities but to replace national investments triaged in favor of debt repayment. This is