Miller Once Again Opts To Hike Interest Rates

The Fed Chairman's aim is a deflationary recession in the U.S.

Federal Reserve Board chairman and London ally G.W. Miller emerged from a National Security Council meeting called to discuss the slide of the dollar the evening of Aug. 16, to indicate that he will attempt to push up U.S. interest rates, once again. Indeed, on

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that afternoon, Miller pushed up the federal funds target rate — the rate at which banks trade overnight money — to 8 percent, up from the 7.875 percent level the day before, and there were press rumors that the discount rate would be jacked up to 7.75 percent.

However, it soon became apparent that despite Miller's intentions, it was by no means evident that his interest rate increases would stick. By late afternoon of Aug. 17, the federal funds rate had dropped to 7.94 percent. Moreover, the yield curve showing the difference between one-month and one-year Eurodollar securities remained unchanged all week: one month Eurodollar rates were 8.19 percent on Aug. 14 and 8.37 percent on Aug. 17, whereas one-year Eurodollar rates were 8.94 percent on Aug. 14 and 9.125 percent on Aug. 17. If traders had expected Miller's increase in short-term rates to stick, money would have shot into short-term instruments and the yield-curve this week would have narrowed.

Miller Bids for U.S. Deflation

Miller promoted his latest attempted round of interest rate increases as necessary to strengthen the dollar. In reality, however, the Miller interest rate increase is a barely disguised attempt to trigger a deflationary recession in the U.S., a coherent part of a larger British operation to collapse the American economy and the dollar and force the U.S. to become a regulated satrapy of the International Monetary Fund.

Miller justified his interest rate tightening on the grounds that it was needed to slow the growth of money supply. Miller was supported — and *preempted* — in his "money supply" analysis by the British-linked U.S. press corps and its London counterpart; and by several British-connected or "fiscal-conservative" economists. The most prominent example of this is the London *Financial Times*, which in an Aug. 12 editorial, entitled "Dollar in Trouble Again," recommended that, "In fact, the main threat to world trade is not the falling dollar but so-called policies to deal with it....Mr. Miller is unwilling to make monetary policy the spearhead of the thrust against inflation." Two days after the *Financial Times* editorial, the Italian *Corriere della Sera*, the Swiss *Neue Zürcher Zeitung*, and the *Wall Street Journal* all carried editorials with exactly the same line. Concurrently, Miller reversed his monetary "softness" and became suddenly a monetary hard-liner.

Any Four-Year-Old Would Know

Yet the crux of the "cut the excess money supply argument" is not only unsound in fundamental economic perspective, but doesn't even accord with the fact of the direction of the monetary aggregates. The four week aggregate average of M1 money stock stood at 1.9 percent and the eight-week average was 3.9 percent. The fact that the 26 week average had been 6.8 percent means what any four-year-old child could understand: money growth is *decelerating* not accelerating.

As yet undaunted by this fact, the July-August issue of Bank of Chicago's *First Chicago World Reports*, in an article entitled, "Capital Outflows Help Sink the Dollar" predicted that excess money supply — and the lack of an energy bill — has led to a simultaneously large trade deficit and capital account deficit in both the fourth quarter of 1977 and the first quarter of 1978 (combined trade and capital account deficits of $13.2 and $13.9 billion respectively). The First Chicago *Report* — including several charts, a graph and much verbiage — contends that a simultaneous trade and capital account deficit is an anomaly only explainable by excess money supply, since the existence of a *deficit* in trade usually implies a *surplus* in capital account and *vice versa*. On consideration of the current period, however, the First Chicago analysis turns out to be a tautology which explains little.

Under the current situation, the widening U.S. trade deficit, combined with British-instigated antidollar warfare, had stampeded many multinational corporations and governments to move out of dollars into other foreign currencies, the deutschemark, the Swiss

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franc, etc., and hence the cause of the current capital deficit.

Europe's View

The perception that money-supply cuts are the foremost means to stabilize the dollar is not shared, however, by leading Europeans. According to sources in the West German Finance and Economics Ministries, the West Germans were very relieved by the report that U.S. Secretary of State Vance opposed, at the Aug. 16 National Security meeting, using interest rate hikes as the means to prop up the dollar.

Still, many confused or British-connected spokesmen continued to pour out antidollar propaganda. Robert Norris, president of the National Foreign Trade Council, a New York-based business organization, told the Aug. 17 *Journal of Commerce*, "the need to reduce and bring inflation under control is our nation's top priority." He added that there should be "support actions by the Congress to maintain the strength of the dollar by reducing the budget deficit" — a move which will produce a deflationary credit crunch.

— Richard Freeman

The Press Campaign of Disinformation on the Dollar

Financial Times, *London, Aug. 12, editorial: "Dollar Again In Trouble"*

It is however, one thing to warn of the possibility of intervention, and quite another to welcome it or consider it necessary. In fact, the main threat to world trade is not the falling dollar, but the so-called policies to deal with it. In a longer-term context, the surprising feature of the dollar exchange rate is not the recent fall, but how late it was in coming. . . .

A policy of allowing the dollar to move with market forces has sometimes been labeled in the U.S. "benign neglect," a phrase which has come in for excessive abuse. . . .

Even then however, the international value of the dollar is still important for the U.S. authorities as a domestic inflationary indicator. The external and internal value of the dollar are much more closely connected than most U.S. economic forecasters suppose — a fact which would be demonstrated unmistakeably if the OPEC countries move from dollar pricing to pricing in terms of a basket of currencies. . . .

The fashionable view of the fall in the dollar is that it is due to U.S. energy imports. . . . More fundamentally, the root of the falling dollar is probably to be found in an overexpansionary U.S. monetary policy. It is no accident that the latest bout of dollar weakness coincides with signs that the new Federal Reserve President, Mr. William Miller, is reluctant to make monetary policy the spearhead of the thrust against inflation.

First Chicago World Report, *"Capital Outflows Help Sink the Dollar," July-August edition:*

The much publicized U.S. current account deficit emerged during the first quarter of 1977; the less publicized capital account deficit appeared in the second quarter....

The unwillingness of the private sector to hold dollar assets obviously reflected the judgment that potential risks outweighed possible returns. Interest rates in the U.S. were too low and the probability of continued dollar weakness too high to justify investing in the United States. Both these reflected the more basic judgment that U.S. money supply — driven in part by the expanding budget deficit — was too fast to be consistent with stable, non-inflationary growth.

The solution to the inflation problem can also be simply stated: reduce federal deficit spending and the rate of monetary expansion.

First Pennsylvania Bank, Money Markets, *newsletter, "The Market Assesses Bonn," Aug. 10:*

The lack of any significant policy initiatives coming out of the seven nation economic summit conference held in Bonn on July 16-17 no doubt triggered the latest round of dollar selling. The market was clearly disappointed in an all too familiar way. . . .

It only took about a week for the market to assess the pronouncements from Bonn and the assessment was dramatic. By August 4, the dollar was down 7 percent against the yen from its pre-summit value.

Wall Street Journal, *editorial, "A Dollar Primer," Aug. 14:*

To start to understand what's happened to the dollar, you have to array the accounts to relate both trade and capital movements. While the effort is bedeviled by technical issues, the most sensible resolution we have seen is that used by the First National Bank of Chicago, for example, in the current First Chicago World Report. . . .

The reasons for this (capital) flight are anything but mysterious. In 1977, the U.S. moved to a more expansionary monetary policy, creating dollars faster than it did in 1976 or 1975. By contrast, Japan, Germany, France and Switzerland slowed their monetary growth. This meant that the dollar was bound to lose purchasing power faster than other major currencies. Investors inevitably looked into this account and moved into other currencies. The dollar fell not primarily because the U.S. imported too much oil, but because the U.S. created too many dollars.

The London Observer, *"The Rise and Rise of the World's Share Markets," Aug. 13:*

Wall Street has seen the Dow Jones index push

forward more than 20 percent to 890 since the low of last Febuary. . . .

What is puzzling at first sight is that the rise should have taken place when the consensus of economic opinion is... that the United States is now headed for contraction as the government takes action to curb inflation. . . .

Financial Times, *Aug. 18 article by Samuel Brittan: "Myths About Exchange Rates"*:

Seven years ago I was recalled from holiday because President Nixon had suspended the convertibility of dollars into gold and imposed an import surcharge — as well as imposing wage and price controls. The parallels are ominous. It is August and the dollar is again under pressure, the U.S. President has asked for top level studies, and the weekend after next I shall be passing through Salzbourg — the place from which I was recalled in 1971. This time the main cause for worry is not the falling dollar, but the supposed remedies for it — whether central bankers and central planners share a common distaste for exchange rate movements, as do the businessmen who would like stable exchange rates in an unstable and inflationary world. As a result of these prejudices (i.e., for fixed exchange rates), and a certain misinterpretation of economic research and teaching, it has become fashionable to say that (floating) exchange rates don't work. This still seems to me an attitude devoid of all merit, and a thought which could do untold damage to world trade.

EMS Negotiations At A Crossroad

British efforts aim at creating antidollar 'parallel currency'

Britain made no bones about its opposition to the creation of a new European monetary arrangement as outlined at the July 6-7 European Community summit meeting in Bremen, West Germany. Now London, together with its customary allies in the Belgian

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government, is attempting to skew the European Monetary System (EMS) from inside the negotiations, toward deployment of an antidollar "parallel currency."

What is at stake is the character and purpose of the new European Monetary Fund (EMF). Both the final communique at Bremen and statements at the time by West German Chancellor Schmidt blueprinted a two-part fund. The first part would be a pool of European currencies to be used for coordinated intervention in the foreign exchange markets on behalf of the dollar.

The second, a pool of 20 percent of each member's dollar and gold reserves, would involve the creation of European Currency Units (ECUs), which member central banks could hold. Its key features, however, are (1) a de facto remonetization of gold, as acknowledged by both the advocates and opponents of such a move, and (2) the possibility of redeploying foreign-held dollars — augmented by cooperation with the Arabs — in the form of long-term, low-interest development credits to less-developed countries and the socialist sector.

These dollars would in good measure flow back to the U.S. as payments for industrial and technological exports, reversing the U.S. current accounts deficit and decisively expanding the volume of hard-commodity trade volume conducted in dollars, thus securing and indeed upgrading the dollar's reserve-currency status.

This potential was underlined at the time of Bremen by the leading West German business daily *Handelsblatt*, which foresaw the European Monetary Fund issuing long-term gold-backed dollar -denominated bonds to expand its own lending base. The French equivalent of the *Wall Street Journal*, *Les Echos*, described the fund as *un avaleur des dollars*, a dollar-swallower which to be effective must go beyond central bank-style clearing operations.

Tolerating the British

Thus far, however, the French and West German architects of the fund have to all appearances allowed their conception of the EMS as a seed-crystal for a new development-geared world monetary system to remain the guiding light of a small policy making stratum at the top. The negotiations appear to be afflicted by subordinates' tendency to act as if the EMS were chiefly an affair of the European Community, and to parley with the British as simply another, if troublesome, member of the EC instead of a self-proclaimed saboteur of the dollar and of global industrialization. This state of affairs in turn disorients those in the U.S. seeking genuine dollar support.

West German Finance Minister Hans Matthoefer's Aug. 10 interview with the Bonn *General-Anzeiger* is a case in point. Played down nationally and internationally, the interview was closely read in Bonn and other capitals. Matthoefer's inability to stress the dollar-lending potential of the EMS left him portraying it as a European "bloc." From that point of view, it was naturally difficult to explain how the EMS will