Is a U.S. recession necessary?

Britain's mouthpieces say yes, but sane Americans disagree

Signs of a U.S. recession did indeed accelerate this week along with interest-rate increases, as the National Association of Homebuilders projected a 25 percent cut in 1979 housing starts and the Commerce Department anticipated a large cut in other construction as well. This disintegration of the nation's biggest sector would hit the entire economy at a time when other key props, auto sales and consumer spending in general, look ready to dry up.

But there is nothing inevitable in this depression prospect, since there is no necessity for the interest-rate jackup. On the contrary, the most prudent bankers and officials in Western Europe and Japan expect the new European Monetary Fund's long-term, low-interest operations to start revamping the entire world credit cost structure this January. And, as documented below, some well-placed strategists in the U.S. government and banking community have finally begun to orient toward the EMS, and the self-expanding investment and new export markets it it designed to generate.

Despite mere reality, however, information channels in the U.S. are still utterly dominated by spokesmen who act as if the United States economy were being struck by a blizzard of meteors and everyone can only dig in and watch the rubble pile up. They are more and less witting advocates of a conspiracy — signaled in the British press for the past eleven months, and laid out in full in a secret Bank of England-commissioned memorandum this past August (first brought to public light in this *Review*). The aim is to eradicate for good the American industrial potential — and potential to technologically transform the world — that has merely been curbed up to now by the London-based networks and their U.S. collaborators, whose financial and "geopolitical" power will evaporate should the U.S. join the EMS in a global development policy. They now hope to throw U.S. business into an uncontrolled collapse that will justify International Monetary Fund "surveillance," ensuring that, like the IMF's Third World victims, the U.S. will be "deflated" into permanent invalidism. Trade war and military mobilization would then, according to the scenario, abort the EMS itself.

Press, pundits egg on collapse

The Nov. 6 Wall Street Journal *cited fears of a "19th century panic" and Miller-Blumenthal decision-making as the source of the dollar package, barely noting any U.S. allies' role and ignoring their intent to save the American economy as well.*

. . . Pessimism about the dollar and the administration's economic management had become so rampant that the nation was on the brink of, in the words of one New York banker, "a 19th Century kind of financial panic" from which a genuine depression could have developed. . . .

By Friday, Oct. 27, currency trading had turned so feverishly against the dollar that Mr. Blumenthal felt compelled to see the President — alone — and recommend "strong action."

. . . About 10 p.m., President Carter's helicopter landed on the south lawn of the White House. Charles Schultz, chairman of the President's Council of Economic Advisers, sneaked past reporters who had been with Mr. Carter on his campaign swing in New England. (The next night) the officials met in the White House basement. By midnight, their conclave broke up with a "tentative go-ahead.". . .

The Nov. 6 New York Times *foresaw interest rates slacking only after collapse or credit controls:*

Interest rates, already at their highest levels in four years, will continue climbing and could lead to a severe shortage of credit for business borrowers in coming months, according to money-market economists and bankers.

A consensus appears to be taking shape among them that a replay of the "credit crunch" of 1974, when rates increased to record levels, is a strong possibility. . . .

"Short-term credit demands are soaring," declared one New York banker yesterday. "You're getting demand from the business community, from consumers and from housing, where the demand still remains massive."

The 12-percent (prime rate) level might not be reached, however, if one of two events takes place: a sufficient weakening of credit demands, or a move by the Government to limit credit expansion by imposing outright controls on this sector of the economy. . . .

The Times *business section assembled the following report Nov. 8:*

. . . "President Carter has opted for a recession," writes Sam I. Nakagama of Kidder, Peabody & Company. . . .

Here is what Mr. Eckstein's Data Resources, in Lexington, Mass., is telling its clients, which include many of the largest companies in the United States, as well as some Government agencies: "Interest rates are at a point where housing activity will drop for lack of mortgage money and because of prohibitive rates. Consumer purchases to automobiles and other big-ticket items will be hurt by tougher credit terms, including shortened maturities. Business outlays for plant and equipment will be held down by weaker industrial markets and financial uncertainties."

London: 'danger of mass panic'

The Sunday Times *of London termed the dollar support package a British model plan, and enumerated every possible "sickening prospect" for the world economy, including U.S. currency controls, in an article titled "This time the wolf is really at the door":*

. . . If the package President Carter launched last week fails to save the dollar the world's money system would collapse and with it the prosperity of the western economies. . . .

. . . Listen to this, for example, and you could easily be forgiven for thinking that it was the Governor of the Bank of England. "There are three problems: poor productivity, a declining rate of economic growth, and poor international economic performance, but the real problem is the struggle with the disease of inflation. . . . For a long time officials, commentators, and citizens have routinely deplored (them). . . . But one suspects that few, to use Dr. Johnson's apt phrase 'ate their dinner less well' on that account."

The speaker is the President of the New York Fed, Paul Volcker. . . .

(The package) contained at least three remarkable innovations (including) a loan from the IMF, just like other, weaker nations.

These measures, plus the rise in interest rates to record levels . . . meant that not only was the disease recognisable to British observers, the cure was familiar too. . . .

Even so some experts feel the Administration may have gone too far. Charles Schultz, chairman of the President's Council of Economic Advisers, worries that the high interest rates will choke-off industrial investment and push the American economy into recession.

. . . If the dollar cannot be freely exchanged into other currencies, it becomes even more vulnerable, and with so many hundreds of billions of dollars held by foreigners outside America, there is always a terrifying danger of mass panic.

. . . Oil is at the centre of the other sickening prospect for the world economy. A combination of inflation in the West and the decline of the dollar have already reduced the value of OPEC's oil sales by 30 per cent. Next month they decide how to react. . . .

'I don't see how the EMS can work'

Gottfried Haberler denied in a Nov. 8 interview that the new European Monetary System could avert these crises. Haberler is a founding member of the Mont Pelerin Society, a semisecret "conservative" propaganda and special operations group set up by Walter Lippmann, the London School of Economics, and Friedrich von Hayek after World War II. He is now also a fellow of the equally synthetic, British-controlled American Enterprise Institute.

Q: There has been a lot of controversy swirling around the proposed European Monetary System. Can you give me your views?

A: I don't see how the EMS can work, given the tremendous disparity in inflation rates among the countries who would participate. . . .

Q: There is a lot of evidence indicating that the Europeans intend to use the EMS as the basis of a new international monetary fund. What do you think?

A: It's true that they have plans to set up a large intervention fund, but I still maintain that there will be tremendous difficulties. I just saw a study produced by the Institute for World Economics in Kiel, West Germany, which is highly critical of the EMS precisely because it has no mechanism for resolving the inflation-rate disparity I mentioned above.

Q: How about the U.S. economy? What do you think needs to be done?

A: We cannot stop inflation without a recession. I hope we won't have anything more than a mild recession, but a recession is a definite necessity.

Q: I understand you are a member of the Mont Pelerin Society. Were you at their meeting in Hong Kong last month?

A: Oh yes. The Mont Pelerin Society is a private organization, aimed at promoting the free market economy. We're like the old European liberals, though we're not monolithic.

Q: Was the EMS discussed at the Hong Kong meeting?

A: Oh, yes, at length. . . . There was no consensus. . . . (Friedrich von) Hayek and (Milton) Friedman didn't see eye to eye. . . . If you want to discuss it further, why don't you come to D.C. . . . It's a long story.

Voices of sanity call for exports

In an article headlined "Europe's Move Toward Stable Currencies Causes Enthusiasm, and Concern, in U.S.," the Oct. 30 Wall Street Journal *carried the first specific report of any official U.S. positive stand toward the European Monetary System. (Note that Hinton was involved in replacing pro-British King Farouk with Gamal Abdel Nasser in Egypt in 1952-54.)*

... We think it perfectly possible to work out arrangements in the three areas of our concern" says one American official. Much will depend on the detailed design of EMS. Some U.S. officials, including Deane R. Hinton, head of the American mission to the Common Market in Brussels, are actively enthusiastic about the prospect. Mr. Hinton, for one, has been trying to persuade his colleagues in Washington that EMS can't help but benefit the U.S. over the long run through greater European economic and political stability....

The Washington Post *carried a tiny Associated Press wire Nov. 7 on U.S. State Department support for the EMS. Sources say the official quoted was George Vest, assistant secretary for European affairs. Vest is a foreign service officer with previous experience in NATO and European Community posts.*

The U.S. government hopes a new Western European monetary system will work, and complaints about it from Treasury officials do not represent Carter administration policy, according to a State Department official who asked not to be identified.

Some fear has been expressed here that the European system would threaten the position of the dollar on foreign exchange markets. European officials have sought to allay those fears.

The fight in the U.S. Administration

There's clearly a fight on over the issue. A Nov. 8 interview with Michael Ely in the State Department's Office of Monetary Affairs confirmed State-Treasury battles over the EMS. Ely stressed Treasury's insistence that the EMS will be bad for the dollar.

Q: There's a report in today's Washington Post *quoting an unnamed State Department spokesman expressing U.S. support for the EMS and saying that Treasury complaints about it should not be taken as official Carter Administration policy. Do you know anything about this?*
A: I have no idea who said it....I just came back from a long meeting with Treasury....There were State Department people, including Richard Cooper, and Treasury people there. We agreed that the EMS will get a welcome from the U.S. and that it could be economically good for the U.S.

Q: How about the dispute between Treasury and State on the EMS?
A: There has been trench warfare at the middle level between us...The people at Treasury are worried primarily about the EMS's effect on the dollar, while we think that this concern should be subordinated to our desire for European economic unity.

Q: What happened at your meeting today?
A: We sat down and looked at all the problems involved....We agreed that the Europeans don't want to hurt the dollar, and don't want to undermine the IMF. We believe that the interests of the Europeans and the U.S. are the same. Of course, Treasury will remain watchful...they're still concerned about the dollar.

Q: How can anybody maintain that Treasury is worried about the dollar? They've been the most notorious proponents of the malign neglect policy.
A: Well, it is true that up until a week ago the Treasury wasn't concerned about the dollar....

Q: It's my understanding that it was State, and Vance in particular, who forced through the Administration's dollar support operation under European pressure.
A: Well, I was scared to death myself last week at the dollar situation, and I wish I could say that State was responsible for Carter's action, but to tell you the truth, no one who could have pushed it through was around last week....

On Nov. 4, the same day that First National Chicago bank chairman Robert Abboud called on CBS radio for capital formation and "export or die" measures to follow up the Carter dollar stabilization plan, Democratic Senator Adlai Stevenson III of Illinois expanded the point. From NSIPS's Nov. 5 story:

...Stevenson, who has functioned as the leading congressional figure concerned with expanding U.S. export markets abroad, supported the plan as a "short term stabilization." He noted that "while the higher interest rates" component of the plan may "be of immediate benefit, in the long run it may be detrimental to the economy."

The next steps for long-range dollar stabilization, added the senator, would be creating a "program for capital formation and exports...conservation and protection of energy," and lowering "food, housing and other prices."

A speech the prorecession press wouldn't cover

In a speech titled "The Plight of the Dollar" delivered in Spokane, Washington Nov. 2, Bank of America President A.W. Clausen *elaborated on how to achieve the capital formation for productivity increases to expand exports, beat inflation, and rescue the dollar as a world reserve. The speech was not covered by any of the prorecession East Coast press, and indeed, to* EIR*'s knowledge, was reported on solely by U.S. correspondent Horst Seibert in the West German daily* Die Welt, *although the San Francisco-based Bank of America is the nation's largest commercial bank. Excerpts from the speech follow.*

. . . Since World War II, the United States dollar has been the world's key trade currency—the international medium of exchange and store of value. As such, it has helped provide the foundation for an amazing expansion of world trade and remarkable improvements in global living standards.

Such key currencies as the mark, the yen, and the Swiss franc are highly regarded. But the economies underlying them are substantially smaller than ours, and could be overwhelmed by the capital shifts that a reserve currency role almost certainly would impose. Monetary authorities of these countries historically have been reluctant to see the dollar's reserve burden shifting to their currencies. . .

. . .SDRs are essentially a unit of account for use among government bodies. Attempting to extend their use to commercial transactions at present is more of a theoretical possibility than a practical prospect. . . .

Clearly, for a long time to come, the best answer for all concerned is nursing the dollar back to health so it can once again perform its international monetary function in an atmosphere of confidence and stability. . . .

. . . it is vital that the multilateral trade negotiations now going on in Geneva succeed in removing (trade) barriers—the more the better.

However, as a nation we must also be smarter and more diligent in efforts to stimulate the sale of our own exports. . . .

Unfavorable relative inflation rates, of course, raise our costs and thus make our prices high compared to those of foreign goods, and this trend makes our exports less attractive while imports become better bargains. To some extent, these adverse movements are offset by the declining value of the dollar. That only spins us into a vicious circle: The plunging dollar raises our costs which add to inflation and, as a result, the dollar declines further. . . .

(On the supply side of inflation's causes) the chief villain is the alarming decline in the productivity growth of our economy. In the Fifties and Sixties, we enjoyed nearly a 3 percent annual improvement in productivity. However, over the past ten years, growth has slipped to only 1.4 percent. . . . a principal cause of our weak productivity improvement has been sluggish capital spending. For instance, between 1970 and 1975, Japan's capital investment as a percentage of gross national product was slightly more than double that of the United States, and West Germany's was more than 45 percent higher. . . .

The return on capital can be improved most readily by redirecting our tax policies. . . . The basis for depreciation could be changed from historical cost to replacement cost, so that businesses operating in this very inflationary environment would no longer have to use after-tax dollars simply to replace worn-out plant and equipment.

The return on capital would also be aided by programs to reduce government's involvement with, and interference in, business activities. The cost to business of simply responding to government regulations and paperwork requirements is monumental—in excess of $100 billion. . . .

We must not let wage and price standards become the centerpiece of the fight against inflation. Similarly, the actions announced yesterday to reverse the decline of the dollar must be put in the proper perspective within the much larger context of the problem . . . against the backdrop of 500 billion of Eurodollars primarily owned by foreigners. . . .

In this final analysis, a nation's currency is a measure of its people. It can be debased or it can be viewed as an obligation and a bond.