FOREIGN EXCHANGE

Dollar's stability is deceptive

At deadline on Feb. 15, the U.S. dollar remained stable within the DM 1.85 to 1.86 band which had characterized the entire week's markets. In contrast to last week, when traders were surprised at the dollar's instability, the New York and Frankfurt markets were dumbfounded at the American currency's failure to react to the seizure of an American embassy in Iran, the murder of an American ambassador in Afghanistan, the announcement of a 7 percent oil price rise by two Persian Gulf states, and reports of conflict on the Sino-Vietnamese borders. However, several of the large London foreign exchange dealers calmly reversed their forecasts of sharp dollar decline, and projected a buoyant dollar for the immediate period ahead.

Traps lie in that direction. All the factors keeping the dollar up — and central bank intervention was the least of them last week — are byproducts of the destabilized international situation itself, to the point that the dollar's stability is a sort of perverse effect.

1) The rise in oil spot market prices and the threat to supplies potentially hurt Western Europe and Japan, and implicitly their currencies, more than the dollar or, for that matter, the British pound. The British view on the matter received an apt summary from Bank of England advisor Sir George Boulton, who argued in a recent speech that Britain, Canada, and Mexico would be the world's growth areas, while Europe would decline, due to its dependence on imported energy and raw materials.

2) Any rise in oil prices produces an immediate technical benefit to the dollar. As long as oil trade is denominated in dollars, any increase in the price of oil automatically increases demand for dollars and net sales of other currencies. The additional cost of oil due to the spot market increases registered thus far adds up to $50 to $100 million per day — more than the average daily foreign exchange market

TRADE

White House threatens Japan with trade war

The Carter Administration is demanding that Japan "reduce its trade surplus" and adopt a package of economic "alternatives" to exports whose only effect can be quick eruption of depression in Japan's heavily export-weighted economy. To back these demands up, Washington issued two heavy-handed threats this week: 1) unless a redress of the surplus is visible immediately, Carter might not attend the crucial June Tokyo Economic Summit of Western heads of state, and 2) the U.S. might allow 15 percent tariffs to be slapped on Japanese imports, now that the waiver provisions of the 1974 Trade Law have expired.

Washington asserts it is acting on behalf of U.S. exporters. On Feb. 11, the New York Times gave heavy coverage to alleged "grass-roots" support for such moves coming from unionists and business leaders in the suffering textiles and steel industries. Nevertheless, the Carter Administration has shown no real commitment to expanding U.S. trade. Its recent attacks on Japan are part of its adoption of the "China card" policy, which also prescribes a very specific role for Japan — drop its industrial development orientation throughout Southeast Asia, in favor of "remilitarization" and Chinese-style agricultural backwardness for the region.

On Feb. 10, the New York Times "leaked" that last December, Carter sent a letter to newly-elected Japanese Prime Minister Ohira, threatening that if the Japanese didn't reduce their trade surplus, Carter might boycott the Tokyo summit. Midweek, the White House continued to refuse to answer reporters' inquiries as to the accuracy of the report.

On Feb. 12, West Germany's conservative Frankfurter Allgemeine Zeitung covered the "leak," adding that Carter — on advice from House Ways and Means Trade subcommittee head Charles Vanik (D-Ohio) — was threatening not to renew the 1974 import tariff waivers. Vanik has been publicly adding fuel to these threats by issuing public statements asserting he expects a "big fight" in Congress over this issue.

Similarly, during a conference in

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intervention by central banks during the past two months.

3) The instability of the credit markets following the collapse of the Bakhtiar government in Iran is, possibly, the most significant factor temporarily weighing in the dollar's favor. The Dow Banking Corp. of Switzerland has already successfully enjoined a small Irani private bank from withdrawing its deposits held at New York's Chase Manhattan Bank and at various London banks, claiming default on interest on Dow's deposits at the bank. The London Financial Times of Feb. 14 projected a wave of activations of default clauses on commercial bank loans to Iran. Almost certainly, the Financial Times report is premature; one New York lending officer qualified the report as "panic-mongering." There has been widespread speculation since early January that commercial banks might exploit the occasional dysfunction of the Irani central bank, largely due to strikes, to seize Iranian deposits. No such action has been taken from the New York side. The West German Economic Ministry released a statement Feb. 13 insisting that there would be no moratorium on DM 12 billion on outstanding West German debts to Iran.

However, exaggerations aside, the Eurocurrency market situation is potentially serious enough to make what is usually called a "surplus liquidity" situation look barely comfortable. Apart from Iran's own $12 billion foreign debt, the current account balances of non-oil LDC's look considerably worse in the light of another oil price rise — a point emphasized by Bundesbank chief Otmar Emminger in a press statement Tuesday. The reduction in the flow of crude knocked the bottom out of an already saggy tanker market, pushing the Worldscale index from about 28 — what is considered the breakeven rate for operation of a VLCC — to about 20 at the beginning of last week. The implication is that the weakest borrowers in the market, including those who had stabilized their positions over the past year, including tanker operators, are now significant short-term borrowers. The slight firming of Eurodollar three-month rates (at roughly 11¼ percent at deadline) probably has more to do with this than with the opening of new short positions against the dollar.

All of these factors, although they act to temporarily firm the dollar, belong to a pattern that adds up to grave danger for the dollar credit system generally. Europe's central bankers, who saved the dollar on several occasions — from the jaws of Michael Blumenthal and James Schlesinger — are not hiding their frustration at American policy. At a Feb. 14 conference in Frankfurt sponsored by the London Financial Times, both West Germany's central bank head Emminger and Danish central bank governor Erik Hoffmeyer told the EIR that they did not believe it possible to create a stable currency relationship to the dollar unless something basic changed.

—David Goldman

Washington, D.C. sponsored by the Japanese newspaper Nikkei last week, U.S. spokesmen attacked Japanese international and lending policies. In coordination with West European bankers and poltical leaders, Japanese banks have been issuing multibillion-dollar, dollar-denominated loans in Tokyo to finance important industrialization projects throughout Asia. These loans, created by the enormous pool of surplus dollars held by both private and public financial institutions in Japan, are being given, to the horror of U.S. and British banks, at interest rates well below prevailing Eurodollar interest rates.

During the Washington conference, Brookings Institution "Japan watcher" Philip Trezise proposed that the Japanese use their surplus reserves to back up a new printing of yen, and create a yen-loan market, or "bloc" in Asia. Just like the West Germans, the Japanese have firmly rejected "internationalization" of their currency, on the grounds that it would fuel inflation, and that the emergence of competing "currency blocs" would cause massive disruption of trade worldwide. In proposing the yen bloc, Brookings also foresees the Japanese deemphasizing their financing of industrial development, in favor of funneling loans in Asian "hot-money" markets — ranging from the Hong Kong stock market to Singapore real estate.

In a private discussion, however, Tresize admitted that Carter's recent resumption of a "gloves-off" posture toward Japan has not borne out successfully for Washington.

The Japanese, he predicts, will simply strengthen their ties with West Germany, in preparation for forming a front against "the UK, U.S. and Canada" at the Tokyo summit.

Other reports indicate that indeed the Japanese are getting hopping mad about these U.S. efforts at blackmail. The Feb. 12 Frankfurter Allgemeine Zeitung also reported that a leading Japanese think tank has prepared a special "still confidential" proposal for the government to present at the summit gathering. As described by the Frankfurter Allgemeine Zeitung, it calls for a new international monetary system to be founded on the model of the just-created European Monetary System (EMS). The EMS, often mischaracterized as strictly an internal European "currency stabilization" mechanism, is an ambitious program for the founding of a European-wide bank which can issue massive, dollar-denominated loans, particularly to Third World countries, for industrial imports and technological advancement.

Observers have also seen it as a sign of Japanese hardening towards the U.S., that on Feb. 13, Prime Minister Ohira publicly asked his opponent, former Prime Minister Fukuda, to go to Washington as a special emissary to negotiate problems of trade. Fukuda is recognized as a spokesman for Japanese industrial interests which are in closest contact with West Germany and France on the EMS monetary reform moves.

— Renee Sigerson