DOMESTIC CREDIT

Fed Chairman Miller to pull the plug

In remarks to a luncheon meeting of the New York Financial Writers' Association on July 18, Robert H.B. Baldwin, president of Morgan Stanley, Inc., warned that a "soft landing is not in the cards" for the U.S. economy in 1979-80. He also predicted a period of even lower volume of new stock and bond issues in the nation's capital markets and vociferous competition among securities firms and banks over the dwindling business. Mr. Baldwin is the "Cassandra of the securities industry" who in 1974 predicted that 150-200 firms operating on the New York and regional exchanges would shortly go out of business—which indeed they did.

The monetary course outlined by Federal Reserve Chairman G. William Miller before Congress July 17 virtually ensures the sort of "hard landing" later this year foreseen by Mr. Baldwin. Miller said that the economy has entered a recession, which will be a lot deeper than the Carter administration spokesmen think. Miller, at the same time, assured the House Banking Committee that the central bank would resist pressures to ease monetary policy in response.

Seasoned Fed-watchers and stock market investors are reading Mr. Miller's remarks as the signal that the Fed is going to tighten monetary policy at this time—that Miller is pulling the plug on the U.S. economy. The rationale for this policy decision will be the dollar's uncontrollable slide on world foreign exchange markets following the fiasco of President Carter's Sunday night energy address and the multiplying confusion in Washington.

The monetarists at Citibank pin the blame for the dollar's recent troubles principally on U.S. monetary policy, which they say has become less restrictive than it was during the post-Nov. 1 period. Between approximately last October and May, the U.S. monetary base (reserves supplied to the banking system and cash in circulation) was growing at a 6-7 percent annual rate. In the last six weeks, it has sped up to an annual rate of 9-10 percent. Predictions are now rife that Miller is about to return to his pre-June stance.

Interest rates are already headed up again in response to expectations of future Fed policy. At the weekly

CORPORATE STRATEGY

Computer industry shakedown?

The interconnections of three big corporate stories in the past week got fluffed over by the financial press. They were the International Telephone and Telegraph (ITT) shakeup, the shift in International Business Machines (IBM) marketing strategy, and the Lloyds of London payout to computer leasors whose contracts were terminated.

At stake is whether the electronics sector will become the leading edge of turning high technology into a war machine. The ITT and IBM shifts are in this light best compared with the recent changing of the guard in the British government, followed by a campaign on the part of Margaret Thatcher and her fellow "Black International" spokesman, Franz-Josef Strauss of West Germany, for a huge push in the microchips and data processing fields.

The other side of this militarily-oriented drive is economic warfare against Japan and secondarily, France. IBM intends to capture the entire equipment market for the increasingly integrated data processing, telecommunications, and computer market, instead of merely the computer or small machines end of the industry. It will speed up its introduction of new technologies for this purpose, abandoning its traditional "you'll buy when we decide to market" approach. This is geared to impose an "office of the future" electronics mode, geared toward the military, toward bureaucracies, and surveillance and manipulation of business—instead of developing the field's industrial and educational applications. Together, IBM and ITT are out to lock up control of strategic national telephone and telegraph systems around the world, and indeed all aspects of digital and voice-grade communications.

ITT shakeup

On July 11, the ITT board of directors sacked Lyman Hamilton, president and CEO since 1977. His replacement, Rand V. Araskog, West Point '53, was a special assistant in the McNamara Whiz Kids' advanced research agency at the Defense Department. After stints at Honeywell and ITT's Federal Laboratories, a top government contractor, Araskog was named president of ITT Defense Communications, and rose to EVP by 1976. He is a top

Treasury bill auction on July 16, interest rates rebounded to their highest levels since June 4—the rate on the Treasury's 26-week bills rose to 9.255 percent and the rate on 13-week bills went up to 9.336 percent. Several weeks ago, we predicted that when the impetus for higher rates appeared, T-bill rates would go up just as fast as they came down in the first weeks of the summer, due to the leveraging effect of the Treasury bill futures market. This is precisely what has happened.

Since Carter's Sunday night address, yields and prices in the bond market have been reflecting investors' jitters over the mess in Washington—and yields are generally up and prices down.

The most revealing statement in Chairman Miller's July 17 speech was what he had to say abut the relationship between monetary policy and the recent oil-price hike: "If we tried to accommodate it, we'd unleash more inflation. If we tried to overreact to it and send the economy into a tailspin, we would just open ... more problems. As usual, we proceed with proper balance, perspective and brilliance" (sic). Miller's promise here that he will not finance the $100 billion oil price increase (in the U.S. alone) through the expansion of credit and money means that the oil price hike will fall as a direct tax on industry, agriculture, and U.S. living standards.

In his address to the NY Financial Writers' gathering, Morgan Stanley's Robert Baldwin was negative about the synthetic fuels program presented in the president's benchmark energy speech. Baldwin cited the long lead time and galloping costs involved in the construction of South Africa's coal gasification plants, which he recently visited, and hinted that the private capital markets want no part in financing the president's "ambitious" proposals. This view is particularly interesting from the head of a firm which did the financing for such major projects of the postwar period as Churchill Falls and the Alaskan Pipeline and is now involved in a big way in financing Australian oil shale production. Morgan Stanley is also the principal investment bank of most of the major oil companies. Perhaps Baldwin is saying that the private sector will only throw its support behind synthetic fuel production when the conditions are right: when the profitability of synthetic fuels has been ensured through the U.S. population's acceptance of "conservation" and fully decontrolled oil prices as a way of life and through complete government guarantees for private investment.

—*Lydia Schulman*

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operating man in the style of ITT board chairman Harold Geneen, with a full background in high-technology military applications and espionage capabilities.

Geneen himself announced July 18 that he is putting together a venture capital group along with unnamed bankers in Munich (Strauss's home base), Lazard Frères' Felix Rohatyn, retired Alcoa chairman John D. Harper, and Henry L. Hillman of Pittsburgh. Geneen, who reportedly opposed Hamilton's policy of lopping off ITT's earlier acquisitions, is not exactly launching a "private" project, however. Such "venture capital" setups are simply fronts for ITT and IBM; in this case, no one is likely to think otherwise.

The ITT shakeups are complemented at IBM. In the second quarter of this year, IBM announced a rare earnings drop and a still rarer intention to borrow $1.5 billion. This borrowing, it was explained, is to augment the $4 billion cash appropriation for the new computer leasing system that will entirely reverse IBM's marketing strategy. Instead of slowly unveiling a succession of big computers and refinements on small office machines, IBM will use its immense resources to crunch competitors.

Those "competitors," like Amdahl, have merely operated to test the waters for IBM's new push. The real targets are companies like Itel, which markets the large Hitachi AS/8 against IBM's yet-to-be-produced H series. Once IBM has beaten Japanese marketing toeholds in the U.S.—Japan has been largely terrorized or prohibited from directly marketing advanced computers in the U.S.—it will, with ITT, take on the Japanese and French national phone systems, which provide R&D capital to domestic electronics and telecommunication companies.

The Anglo-American electronics operation wrecked France's computer industry in 1974 by pulling Philips out of the European computer partnership. The Japanese have continued to develop the most advanced technology on a scale sufficient to broadly apply computerization to industrial processes. Since this would reverse the "limits to growth" commitment of the IBM forces, IBM and Washington, D.C. have moved in for the kill.

Lloyds of London is part of this deployment. Even if it pays as much as $1 billion to computer equipment leasors, Lloyds will not go bankrupt, contrary to *Wall Street Journal* and industry analyst rumors. Lloyds' payouts will liquidate industry debt, indirectly freeing IBM to float its new leasing arrangement. IBM will have plenty of resources for its marketing blitz: on top of the $4 billion kitty and the $1.5 billion credit line, pension funds, insurance companies, and offshore funds like Britain's GT Management are jointly moving a lot of money into electronics.

—*Leif Johnson*