Business Briefs

European Economies

The failure of monetarism

The economies of Europe have reacted to the adoption of monetarism by their own central banks and the Fed with a pronounced economic downturn in the fourth quarter. At the same time, inflation is out of control, despite the war against it, which was the excuse for the monetarist credit squeeze.

The European Community this week announced this week that consumer prices in the EC nations rose to 14 percent during 1980, compared with 8.6 percent in 1979. In Italy, consumer prices were as high as 21 percent. Italian prices accelerated at year's end to a 25 percent annual rate in November.

The West German economic miracle is suffering the worst downturn. The Federal Statistics Office announced this week that real Gross National Product fell from a 4.5 percent rise in 1979 to a 1.8 percent rise during 1980, close to zero growth.

In Holland, unemployment rose to a postwar record of 302,000 during December, up from 205,700 in December 1979.

In Britain, Europe's premier monetarist economy, new car sales dropped by 11.8 percent during 1980, the Society of Motor Manufacturers announced.

East-West Trade

Poland gets major West German credit

Poland has accepted a West German government offer of export credit guarantees totaling 300 million deutschemarks, Reuters reported this week. The German government may pledge up to 700 million marks pending discussions between Polish and Western government officials in Paris Jan. 16, sources said.

The loan guarantees are meant to stabilize the unsteady Polish economy and simultaneously to promote East-West trade. About three-quarters of the credits must be tied to purchase of raw materials and semi-finished products needed by Polish industry, hard hit by strikes and other unrest, and the rest to Polish food imports from West Germany.

Polish foreign trade ministry officials visited Bonn earlier this week to discuss additional loans.

The Polish finance minister, Marian Krzak, meanwhile told Reuters that Poland has no intention of declaring a debt moratorium, but seeks to encourage continued East-West lending and trade. "The main thrust of our activities is to secure new credits, and in many countries a moratorium automatically entails the suspension of additional credits.

"However, if one of our creditors were to suggest a moratorium on repayments while offering guarantees of additional credits, that would be an offer no one could refuse," said the minister, adding that Poland is not asking for a moratorium.

Poland's foreign debt is currently estimated at $24 billion, and Poland is faced with a debt-servicing charge of between $8.5 and $9.5 billion, he said.

Corporate Profits

Volcker squeezes fourth-quarter figures

Federal Reserve Chairman Paul Volcker's credit squeeze has had a serious effect on both fourth-quarter corporate profits and those for the whole year.

The rise in interest rates from 11 percent to 21½ during the last quarter means that most major U.S. banks will show a profit drop in the fourth quarter, Wall St. bank analysts forecast this week. "There will be varying degrees of disappointment" in the figures, Robert Alberson of Smith Barney Harris Upham said. Banks suffered a squeeze on margins, as their costs of funds in the federal funds market rose faster than their ability to raise lending rates to customers.

Citibank in particular is forecast to suffer a 12 to 15 percent drop in fourth-quarter profits, because its large consumer-loan portfolio yielded a fixed rate of return while the cost of funds rose.

The homebuilding and auto-supply sectors are also being badly hit. Champion Home Builders Company of Michigan this week forecast a flat loss in its fourth quarter, ending Feb. 27, because high rates destroyed the home-purchase market. The Borg-Warner company announced its 1980 earnings fell to $5.5 a share from $7.25 in 1979 because "depressed auto and housing markets cut earnings deeply." Borg-Warner produces machinery and construction equipment for the auto and housing industries.

International Credit

Eurobanks go fishing for the IMF

Seven leading international banks based in London announced Jan. 7 they will be issuing large certificates of deposit denominated in Special Drawing Rights (SDRs), the fiat currency circulated by the International Monetary Fund. The CDs will be offered to multinational corporations, central banks, and investment portfolios to "protect" depositors against the uncertainties of currency fluctuations.

SDR deposit acounts have existed in London for a few months, but the CD market was set up in the aftermath of the Jan. 1 introduction by the IMF of a different "composition" in the SDR currency basket.

The fiat paper used to be measured in 16 currencies; since Jan. 1, however, the IMF has reduced the composition to five leading currencies: dollars, deutschemarks, yen, French francs, and British pounds.

According to London reports, the IMF, which usually refrains from comment on technical commercial banking developments, greeted the SDR pool with enthusiasm. The IMF is hoping that a substantial SDR interbank market will develop, in expectation that during 1981 it will seek commercial banks loans on the Euromarkets. The IMF is widely reported to be about $10 billion short of the reserves it will need to meet emergency loan operations for countries in payments deficit this year.

Among the banks which have taken the lead in paving the way for such IMF borrowings is the Hongkong and Shanghai Bank, notorious for its involvement in vast illegal money transfers tied to international narcotics and related trafficking.

Banking

S&Ls hit by high interest rates

The Federal Savings and Loan Insurance Corporation announced that only its last-minute rescue operations, providing short-term credit bailouts, kept 35 savings and loan associations from bankruptcy during 1980. The corporation spent a record $1.3 billion in federal funds to save institutions with total assets of almost $4 billion.

Throughout the nation, S&Ls are suffering a sharp decline in profitability due to the Fed's interest-rate squeeze. Industry analysts say the profit fall has been particularly sharp in California.

Jerry Gitt, an analyst at Dean Witter Reynolds, estimates that net earnings fell an average of 44 percent at the six largest California S&Ls in 1980. Gitt and Shearson, Loeb Rhoades analyst Allen Bortel see only a modest improvement in S&L earnings in 1981, depending on the extent of interest-rate decline.

New loan volume has dried up, old loans are turning over slowly, savings flows are outflows instead of inflows, and the higher cost of funds may continue to hurt earnings through the first half of 1981, both analysts said. Bortel reported that mortgage lending has virtually ceased "because a growing number of S&L executives are refusing to make fixed-rate loans, ever again." This means that savings institutions are insisting on wider use of floating rate mortgages, whose interest rates fluctuate with market rates within certain limitations.

As part of the national turned toward deregulation, the California S&Ls are permitted to offer interest-bearing checking accounts beginning this year, putting them in direct competition with commercial banks. Early reports are that the S&Ls are pricing the accounts cheaper than the commercial banks to gain new customers. But the new accounts may end up hurting the S&Ls. "Many California banks think S&Ls will lose money on the accounts and will only steal bad customers of the banks," Gitt said.

Auto Industry

Fraser: 'Chrysler can't survive these high rates'

United Autoworkers head Doug Fraser emerged from the Chrysler Loan Guarantee Board meeting Jan. 7 to tell reporters: "The Chrysler Corporation cannot long survive in the present economic climate with the horrendous interest rates." As part of its attack on the effect of interest rates on the auto industry, the union has announced its willingness to forego contracted pay increases, on condition that Chrysler's bank creditors agree to the company's request for debt relief.

Chrysler is asking that $570 million in bank debts be converted into preferred stock. If the Loan Guarantee Board approves a new credit line to Chrysler, which is currently asking for $400 million, the company could avoid a shutdown in the near term.

The UAW is urging that Chrysler be allocated the full $700 million remaining in the loan-guarantee pool now, arguing that if interest rates decline by the second quarter, Chrysler will probably have been saved, at least for now.

But in the medium term, Chrysler will not survive without access to new sources of credit. The company's treasury, out of which cash flow and backup for current expenditures are financed, is $1 billion in the red.

Briefly

- **THE BANK FOR** International Settlements in Basel, Switzerland believes that there will be no further easing of the world's high interest rates. European and U.S. central bankers meeting at the BIS for their January conference made its focus a reaffirmation of commitment to a sharp curtailment of central bank credit.

- **HENRY REUSS,** chairman of the congressional Joint Economic Committee, called for a six-month wage and price freeze this week at testimony before the JEC by Bureau of Labor Statistics Commissioner Janet Norwood.

- **OIL IMPORTS** are down 25 percent compared to 1980, in the U.S. American Petroleum Institute figures for the week ending Jan. 2 report that daily oil imports fell 294,000 barrels to 4.83 million barrels per day compared to the same period last year.

- **PROF. HYMAN MINSKY** of Washington University in St. Louis predicts "a financial crunch or crisis sometime in 1981, most likely by spring," requiring more Volcker medicine. This will "plant the seeds for a subsequent inflation at rates that exceed recent rates." Reports Leonard Silk in the Jan. 9 *New York Times*, "Curiously enough, President-elect Ronald Reagan's favorite . . . Milton Friedman" also foresees 25 percent inflation in the United States.

- **DREW LEWIS,** transportation secretary-designate, told a Senate Commerce Committee session last week that he will shortly unveil the Reagan administration's program for aiding the faltering U.S. auto industry. Lewis promised that the new administration will not stand idly by and watch the financially troubled Chrysler Corp. "go belly-up." Some regulatory requirements might be eased, he predicted, and action might be taken to reduce interest rates. He also advocated revamping government's role in mass transit.