EIR Economics

After a financial panic: rule by decree planned

by David Goldman

West German Chancellor Helmut Schmidt's July 7 warning, in an interview with the Hannover *Allgemeine Zeitung,* against a "deflationary policy" and "decree government" of the type associated with pre-Hitler Chancellor Brüning 1928-31, should set intelligent observers on edge. A tumble of events is on—some known, some still to be reported—which leads to world financial conditions not substantially different from what prevailed under Brüning's government.

Schmidt, a man not prone to exaggeration, has done his best by way of warning.

To step back for a moment: an article published in this space March 24, 1981, arguing that OMB director David Stockman envisioned a post-panic *dirigisme* of the Brüning variety has occasioned some angry responses from readers who refused to believe that such treachery is possible.

Since this report four months ago drew more controversy than any we published in the past year, it is worthwhile asking: what is Fritz Kraemer doing in charge of Emergency Planning at the Defense Intelligence Agency? What is former Rand Corporation President Henry Rowan doing as chairman of the National Intelligence Council of the Central Intelligence Agency? These two appointments during the past week constitute an apparent mini-coup by the "government-within-a-government" associated with the Federal Emergency Management Agency, or FEMA. Under the last year of the Carter administration FEMA created a parallel structure of administration, expanding from the old Defense Preparedness Agency, and took over actual executive functions in several "emergencies" ranging from the Three Mile Island nuclear brouhaha to the financial side of the November 1979 freeze of Iranian assets in the United States.

Henry Rowan, now a top aide to CIA director William Casey, played the key role under Carter Energy Secretary Charles Duncan in preparing "emergency scenarios" for the eventuality of a shutoff of energy imports to the United States, reaching the conclusion that such a shutoff would be beneficial to the American economy. It would, according to Rand estimates prepared for the Energy Department, compel Americans to stop consuming oil and gas and switch over to coal, and finally convince the United States population that it must make drastic adjustments to deal with the alleged energy crisis.

Fritz Kraemer, the man who invented Henry Kissinger and Alexander Haig during his 30-year encystment at the Department of Defense as the senior civil servant in charge of economic intelligence, is an even more dangerous figure. He is a committed adherent of the

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European circles associated publicly with the remnants of the Hapsburg monarchy and less publicly with the busted Propaganda 2 Freemasonic dirty-money and coup capability in Italy.

If there's no funeral, what are the undertakers doing here?

The shape of the crisis

It is not adequately perceived how close the world is to a major financial blowout. A handful of developments—the shutdown of the Italian stock market for the first time since 1917, the continued rise of American interest rates, the budget crises in West Germany and other European nations, the continued collapse of most commodity prices—have made market participants ill at ease.

For that matter, it is only necessary to read the most recent *International Finance* newsletter of Chase Manhattan Bank and the most recent *Financial Digest* of Manufacturers Hanover Trust to see the unwarranted glibness with which the major banks view the inability of developing nations to meet this year's obligations. Chase has increased its estimate of less developed country (LDC) payments deficits from $50 billion for 1980 to $59 billion for 1981, assuming a drop in export revenues of LDCs due to lower commodity prices and restricted, depressed Western markets; but different and equally reasonable assumptions could produce a deficit forecast for this year in the range of $70 to $80 billion, as Chase's economists well know.

Manufacturers Hanover notes the 50 percent declines in the past year in coffee, cocoa, and sugar, and the 15 percent more price declines in copper and other metals, adding, "In an effort to generate sufficient foreign exchange to pay for higher oil import costs, other necessary imports and the rising cost of debt servicing, many LDCs have increased exports of basic commodities in spite of falling demand and declining prices. To the degree that a particular LDC's exports are concentrated in a single, or a small number of export commodities, these price declines have had a major impact on their domestic economies as well. . . . Many if not most, LDCs are dependent on one or a few predominant exports for a large part of their foreign exchange earnings." None of this is new, certainly not in this publication.

What is new is the extreme likelihood of a wave of major bankruptcies of European banks due to Third World insolvencies and the lack of collaboration of the Bank for International Settlements. We know of one significant institution that last month had to sell off its entire portfolio of gold bullion to raise cash to cover bad debts, and blames the European-wide consequences of the election of François Mitterrand to the French presidency for its own national central bank's refusal to help. With the entire *Landesbanken* system of West Germany showing a loss, the giant Commerzbank missing its most recent dividend, and the German bond market in shambles, the German economy is poised for the same type of crisis that has already blown out the Italian currency and stock market.

There are no important local implications of these developments; the shock waves will exceed those that spread when the Darmstadter Bank closed its doors in 1931.

IBFs the fallback

Almost a year ago, when the American Banking Association and the Reserve City Bankers Association threw their weight behind the New York banks' two-year-old plan for "international banking facilities" to conduct Eurodollar-type business on American soil, it was stated plainly by the proponents of IBFs—and reported here—that the object of the plan was to provide a fallback in case of a crash on the Eurodollar interbank market. The $1.5 trillion Eurodollar market includes about $600 billion of loans between banks, of which the heaviest drawers have been European banks seeking dollars to fund loans to developing countries. A chain of defaults, therefore, threatens not only individual banks, but the banks' creditors down the road.

The big American banks are walking coldbloodedly into this sort of crisis, as the Fed's approval of the international banking facilities (which open Nov. 1) should have made clear. In short, the Fed has stepped over the question of whether it should bail out American commercial banks through the discount window, by obtaining legal sanction to commit the whole public credit to the United States for the defense of the bad loan portfolios of American commercial banks.

Former Chase Manhattan Chairman David Rockefeller is not concerned with a Caribbean "development zone" for altruistic reasons. As we show elsewhere in this issue, the Caribbean is the nexus of the multi-hundred-billion-dollar per year world capital flight market, which Chase has tapped as a source of funding and as a matter of policy since 1966.

The apparent objective of the "international banking facilities" and "Caribbean zone" formats is to erect a *dollar zone* fed by flight capital, including the $70 billion in narcotics-related revenues arising from Latin America, which would stand despite a collapse of the European sector of the interbank market. This implies a global regime of currency *blocs,* a plan advanced in late March by the giant Assicurazioni Generali di Trieste at a conference featuring Prof. Robert Triffin, and since adopted by the Italian and French governments.

Examining the actual dimensions of the Eurodollar interbank market, it is possible to see the mad logic behind David Rockefeller's thinking. As of June 30, 1980, commercial banks in the United States had $185.4 billion in deposits from foreign sources, of which $61 billion were liabilities to banks' own foreign offices, i.e., funding from abroad for loan purposes. The net liabilities to foreigners came to $124 billion.

Of these net liabilities, $20 billion came from Latin America and the Caribbean, and $34 billion from Asia, that is to say, roughly half of the net total came from the two great flight capital centers: the Singapore-Hong Kong axis, and the Venezuela-Jamaica-Bahamas triangle.

The biggest chunk of net liabilities comes from Western Europe, at $61 billion; but of these, two-thirds are from countries whose central banks are virtual arms of the Bank for International Settlements and which would most likely cooperate with the Fed during a crunch. This includes $7 billion to England, over $13 billion to Switzerland, and $3.5 billion to Belgium and Luxembourg, the three European markets closest to the Caribbean-Hong Kong "offshore" nexus.

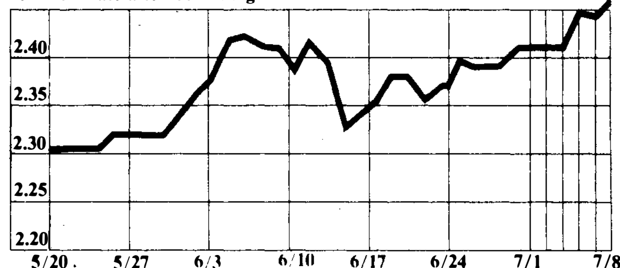
Of course, the creation of a "dollar zone" based on the offshore markets noted could not be handled so easily, but the cited measures give some sort of geographical order and perspective on the size of the actual problem. American banks' loans to Third World countries net of deposits are now, by official measure, $100 billion, and substantially more loans from foreign subsidiaries are figured in; it must be assumed that many of these offshore subsidiaries would be abandoned, and that the Fed would additionally have to buy up between $40 and $60 billion of bad paper.

In other words, the type of "dollar zone" the bankers have in mind as a fallback option, based on the federal printing presses, Latin American narcotics revenues, and other dubious sources of funding, is a prepackaged hyperinflationary disaster. No wonder that international investors are willing to pay 20 percent interest to buy oil and gas in the ground! That they are apparently not willing to buy gold at current low prices is a far more complex issue, treated separately in this issue (see Gold).

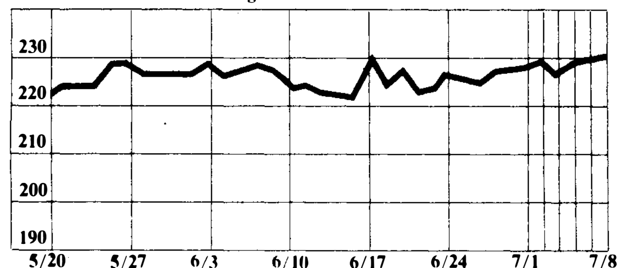
This type of disaster is unmanageable under the stock of methods the Reagan administration heretofore imagined it had available. It implies a highly visible hand directing national economic affairs. Whether the form of the crisis will be the one outlined above is not possible to say; it is only important evidence that leading market participants are following a scenario of this type. Meanwhile, the administration, whether the President knows it or not, is on alert status for economic rule by decree.

Currency Rates

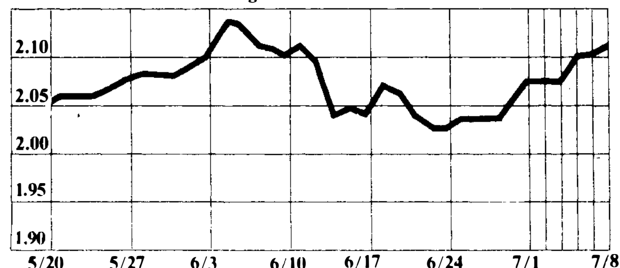
The dollar in deutschemarks
New York late afternoon fixing



The dollar in yen
New York late afternoon fixing



The dollar in Swiss francs
New York late afternoon fixing



The British pound in dollars
New York late afternoon fixing