Reaganomics, Volcker, and the traps of 1981

by Richard Cohen, Washington Bureau Chief

All through the course of 1981, *EIR* issued repeated warnings that the most gaping vulnerability of President Reagan and his administration lay in their initial "Economic Recovery Program"; indeed, all during the late 1980 transition period and into the early stages of the administration, the President and his closest political advisers made it clear that administration foreign policy and international economic policy would be determined by the hub of presidential concern—their domestic economic program.

The importance the President-Elect had attributed to his domestic economic program was made dramatically clear during the transition period, when Reagan spokesmen had warned alarmingly of the potential necessity of declaring an "economic emergency." However, what ultimately came forth as the President's Economic Recovery Program fell far short of what would be required in order to recapture the growth potential of the U.S. economy—and therefore the world economy.

Long before the David Stockman scandal, in which the OMB director revealed to the *Atlantic Monthly* that he knew all along that the U.S. budget deficit would go out of control, *EIR* exposed, through exclusive interviews and analysis, that "supply-side" economics was a hoax directed against both the American economy and the White House. The tax-cut package was designed to facilitate, not capital investment in essential industry, but "postindustrial" writeoffs and flows into "sunrise" and speculative areas. The supply-siders cheerfully revealed that they designed their package to sell the basic Volcker policy of high interest rates and reduced living standards to a pro-growth President.

The stakes

The President's program as it was initially outlined virtually ceded control over the all-important area of monetary policy to the Federal Reserve Board and its Carter-selected Chairman, Paul A. Volcker. Without securing control over U.S. monetary policy and advancing an approach outlined early by *EIR* founder Lyndon H. LaRouche, President Reagan's "economic recovery program" was sure to be doomed.

Critically, the Reagan program failed to advance a reform of the world monetary system that would allow the U.S. government to discipline London-controlled private and offshore markets, as suggested under the LaRouche gold reserve proposal, and simultaneously failed to seize control of direction of the nation's credit by allowing the Federal Reserve Board free rein.

Under the "controlled disintegration" policies for the U.S. and world economy, policies heralded in the late 1970s by a coordinated series of volumes published by the New York Council on Foreign Relations as the *Project for the 1980s* and publicly stated in 1979 by Paul Volcker, popular belief in and government encouragement of unlimited growth and progress were to be considered the enemy—in direct contradiction to the President's viewpoint.

What surfaced during the course of 1981 in a series of battles with the President was the Malthusian anti-growth approach of Volcker, the Council on Foreign Relations, the Trilateral Commission, and their supranational banking arms, the International Monetary Fund (IMF) and the more secretive Bank for International Settlements (BIS), along with their agents within the Democratic Party and Republican Party.

Starting in May 1981, this reporter charged that the vulnerabilities in Reagan's economic policy, once seized upon by his opponents, would lead by the end of 1981 to a series of assaults—including public scandals—against his most trusted advisers, and by 1982, if not remedied, would begin to turn into a full-scale "Hooverization" in the midst of economic disaster.

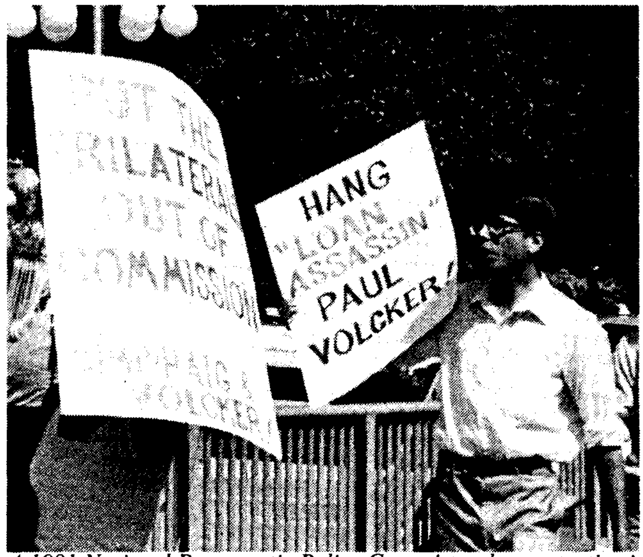
The Malthusians were forced to step up their timetable when they realized that Reagan represented potentially something more than an ideological obstacle to their basic policies of deliberately limited resources, genocidal population control, and global resource allocation.

The combination of the stunning passage of the AWACS arms sale to Saudi Arabia, under the direct leadership of the President, and perception of a potential independent foreign policy tilt in the Middle East, by mid-fall increased the pace of the timetable of assaults against the President.

In addition, presidential recalcitrance against a deafening roar even from within his own party and administration for tax increases and cuts in the defense budget had stirred the Malthusians to more intense activity. While the President clearly does not understand how to get out of the current economic crisis and has shunned intervention against the Fed along the lines suggested by LaRouche, he has, from the vantage point of the Malthusians, also refused to give in on commitments to national defense and the Pentagon and a tax meant to appeal to middle-class "entrepreneurship."

The test

Reagan's somewhat astounding ability to secure enough conservative Democratic votes to pass his first round of budget cuts and defeat a previously boasting Democratic House Speaker Tip O'Neill made headlines in mid-May. However, two days following the astounding victory, major press were touting an alarmed response from Wall Street. Indeed, during that period the stock market had dropped; interest rates had remained stable and were about to climb, completely contradicting the projections of the President's economic advisers. Indeed, *EIR* was the first to report that the Wall Street and Fed reaction was rigged. Alan Greenspan, negotiator for would-be Vice-Presidential nominee Gerald Ford during the 1980 Republican National Convention, along with other former Ford economic advisers and close associates such as former Fed Chairman Arthur Burns, engaged in a process of inciting fear throughout the markets, privately reporting that the President's success meant nothing and that the federal deficit would increase.



NSIPS

A 1981 National Democratic Policy Committee demonstration in Los Angeles.

The Greenspan-Burns actions were coordinated with Stockman, who, operating in conjunction with his collaborators, two days after the great success promoted the astounding proposal for a sizable cut in the Social Security system. In addition, Stockman proposed at that time a series of recissions in the FY81 budget of some $5 billion. White House Chief of Staff James Baker III identified these cuts as needed to offset increased costs due to irregularly high interest rates not projected in the original Carter 1981 budget.

Stockman's shocking Social Security cut proposal was immediately defeated in the Senate 96-0. Yet the actions by Stockman, Greenspan, and Volcker immediately following the initial Reagan congressional success were all aimed at pressuring the President to accept a further deep-cuts policy which in early June would expand to calls not only for cuts in entitlement programs including Social Security, and further cuts in the domestic budget, but also cuts in the projected defense budget and the virtual elimination of Reagan's tax breaks, in order to meet the expense of high interest rates both in terms of direct government interest payments on debt and also loss of government revenue due to the induced recession.

On May 28, Reagan gave a private interview with the New York *Daily News* in which he lashed out at Wall Street's unexpected negative response to his budget cut proposals.

Reagan's move had been encouraged early in that week during a May 24 appearance by House Majority

Leader Jim Wright on national television. There, Wright broke with an announced confrontationist line against the President initiated by House Speaker O'Neill. Wright instead proposed that he and others such as House Ways and Means Committee Chairman Dan Rostenkowski might consider a compromise on Reagan's Kemp-Roth tax bill in exchange for Reagan action on interest rates.

Indeed, Wright brought his proposal directly to the President in a June 1 meeting at the White House. By then, however, it was clear that the President had failed his initial test, rejecting the Wright alternative. As a softener, Reagan obtained Volcker's support of a watered-down version of his tax cut policy. Yet (again as only reported in this journal), two weeks following the Lausanne meeting which had apparently made peace between the President and the Federal Reserve Board Chairman, central bankers—meeting in Basel, Switzerland, at the annual conference of the BIS—issued an outright condemnation of Reagan's policies, charging that high interest rates could only be brought down by a Reagan reversal on tax policy, deeper cuts in the U.S. domestic budget, and an all-out assault on the U.S. defense budget. One week following the BIS meeting, Reagan met with Democratic Senators opposed to Volcker's high interest-rate policy and once again rejected an appeal for bipartisan action.

Containment

Reagan's apparent tax and budget successes during the spring and early summer obscured the fact that he had seriously undercut potential anti-Volcker allies in the Democratic Party and succumbed to a dangerous extent to the deep-cut dictates of the Malthusians; however, during the course of the summer congressional recess, Reagan stood firm against attempts by Stockman and White House Chief of Staff Jim Baker to fulfill one leg of the BIS program—deep cuts in the defense budget.

On Sept. 13, the President announced his opposition to the Stockman approach, calling for only $2 billion in defense cuts for FY82 and $11 billion for FY83 and '84, compared to Stockman's total proposed cut of $30 billion for those years.

Importantly, Senate Majority Leader Howard Baker and Congressional Campaign Committee head guy Vander Jagt, together with House Minority Leader Bob Michel, led a chorus of anti-Wall Street rhetoric that made Reagan's famous interview with the *Daily News* look mild. The Republican leadership—while attempting to keep the interest-rate ball in Reagan's court—were now talking about 90-day time limits within which rates must come down, and serious losses in the '82 election if this were not made to happen.

In addition, close Reagan associate Sen. Paul Laxalt was said to be in negotiations with Sen. John Melcher of Montana, the author of a new bipartisan resolution expressing the sentiments previously put forth by Wright and by Senate moderates, urging bipartisan support for presidential confrontation with Volcker on the interest-rate question. Already Rep. Bill Alexander of Arkansas, a close Democratic associate of Wright, had announced his intention to introduce the Melcher Resolution in the House. There were also strong signs from both liberal House Republicans and conservative House Democrats that the President's coalition for deep cuts would not stand up during the October session.

From the vantage-point of the Malthusian/Volcker/BIS crowd, this combination had to be contained. The elements of containment were already clear at the Sept. 8 meeting of the AFL-CIO-linked National Coalition to Lower Interest Rates. At that meeting, AFL-CIO operatives, under the tutelage of federation President Lane Kirkland, blocked a resolution in support of the Melcher Resolution and instead supported a policy acceptable to Volcker—namely, credit controls.

On Sept. 17 at a national meeting of the Democratic National Committee, the AFL-CIO connected Democratic National Committee Chairman, banker Charles Manatt, challenged delegates who offered a resolution condemning the Fed's interest-rate policies. Manatt insisted that high rates were not to be blamed on Volcker, but on Reagan. The day before, House Speaker O'Neill, an opponent of earlier moderate Democratic attempts to seek a bipartisan front against Volcker, gleefully told a meeting of the House Democratic Caucus, "The monkey is off our back. These are Reagan's deficits and Reagan's interest rates." And on Sept. 19, Kirkland—heavily under the influence of the Socialist International and its representatives in the labor movement headed by International Association of Machinists President William Winpisinger, United Auto Workers President Doug Fraser, and American Federation of Government Employees President Kenneth Blaylock—launched the Solidarity Day demonstration in Washington against the President and his budget cuts. The interest-rate question was infrequently raised there, and when raised, on Reagan, not Volcker.

In late September they succeeded in rallying large-scale Democratic support in blocking the Melcher Resolution from getting to the Senate floor, prior to a much-heralded speech by President Reagan. And, in a meeting of the House Democratic Steering and Policy Committee, Missouri's Rep. Richard Gephardt led a charge of O'Neill-backed elements to block Alexander's attempt to lead a bipartisan move against Volcker (see below). This all-out attempt to contain congressional furor over interest rates on the part of the Democratic Party leadership was flanked by a move coached by Stockman within the administration itself to deflect similar sentiment among Republican congressmen. Indeed, in a Sept. 15 presidential meeting with the Republican House and Senate leadership, the interest-rate question was debated extensively, and Republicans were told that they should keep up the anti-Wall Street rhetoric, but nothing serious would be done at this time on interest rates.

And throughout this period, Volcker, appearing in Brazil in early September and then on Sept. 16 before the Senate Banking Committee, confidently snubbed the Congress and the American people, reporting that interest rates would remain high for at least six months. Already, on the Senate floor, Socialist International-connected legislators such as Bill Bradley (D-N.J.), Ernest Hollings (D-S.C.) and Gary Hart (D-Colo.) were proposing increased taxes in FY83 and 84.

In early September, administration sources were openly admitting what Baker had signaled before—that high interest rates were seriously un-balancing the budget. The previously estimated $42.5 billion deficit for FY82 was now going to be $60 billion. *EIR* predicted at that time that it would be at least in the $80 billion range, as later admitted by the administration.

On Sept. 24, President Reagan responded with his address to the nation, calling for an additional $16 billion in cuts and increased taxes in an attempt to find a middle ground between popular outrage at interest rates and Wall Street requirements for deep cuts.

Power grabs

The Malthusian BIS group happily watched the dissolution of Reagan's majorities in the House and Senate following that Sept. 24 address. The Senate Republican leadership, terrified by the prospect of disaster in 1982, began a campaign to get the President to increase taxes and cut the defense budget. On Oct. 14, Appropriations Committee Chairman Mark Hatfield suggested that the President double his projected cuts for the Pentagon. Ted Stevens, the Majority Whip, suggested the same day that the B-1 bomber program be eliminated. Meanwhile, Republicans on the Senate Budget Committee and Senate Finance Committee, including their respective Chairmen, Pete Domenici and Bob Dole, started to promote a sizable tax increase for FY82, 83 and 84. The pressure increased on Oct. 21 when the government announced a 6 percent drop in GNP for September, followed two days later by an announcement of a 1.2 percent increase in September's Consumer Price Index. Indeed, behind the scenes the word was that the 1982 budget deficit would now be in the range of $100 billion. President Reagan was forced to anounce that a recession had begun. Democrats as a whole were in step with House Budget Committee Chairman Jim Jones, who on Oct. 26 informed his colleagues that yes, the recession is here; Reagan is to blame; we will do nothing until next year.

In the face of what the Malthusians believe to be the irresistible pressure for deep cuts, these forces received a shock when, on Oct. 28, the Senate narrowly approved the sale of AWACS radar planes to Saudi Arabia. Following Reagan's victory on the Hill, he not only seemed to be moving toward a new definition of U.S. Middle East policy, but would stubbornly resist pressures to increase taxes and cut the defense budget.

These factors led to a late-October decision on the part of the BIS-Trilateral trusteeship to quicken the pace of an already prepared all-out assault on the President. The conspiracy to destroy the presidency, and perhaps even attempt once more to assassinate the President, was kicked off when an interview with David Stockman appeared in the *Atlantic Monthly* in which he openly attacked White House economic policy and called for sizable new taxes. While Counselor Edwin Meese and Deputy Chief of Staff Michael Deaver urged the President to remove the heretical Stockman, Stockman's "godfather," James Baker III, stated that Stockman was the most competent official in the administration, and lobbied the President to retain him.

A week after the decision to keep Stockman, a scandal was launched against National Secutiry Adviser Richard Allen. Allen's removal was immediately urged by Baker, with Meese resisting. And one day after Allen went on administrative leave, another scandal was launched through the auspices of nationally syndicated columnists Evans and Novak against Michael Deaver. The pattern was clear. As one Wasingtonian extremely close to the President told me, these series of strenuously pushed scandals (not including the Stockman situation, but now including CIA Director Casey and Labor Secretary Donovan) is aimed at the President himself. And as I have pointed out, the initial goal of this operation, manipulated from the beginning by Henry Kissinger, Alan Greenspan, and the Detroit-based business front for organized crime, GOP fundraiser Max Fisher, was to eliminate the President's closest associates. Political Affairs Director Lyn Nofziger has announced that he will step down in January 1982 after a series of losing skirmishes with Baker. Deaver, now under threat of scandal, has announced that he will also leave in 1982. Allen is effectively gone, leaving only Ed Meese in the White House from among Reagan's original California group. It is also clear that Stockman's revival, and the revival of his policies, was made possible through the auspices of James Baker III. Baker, former campaign director for George Bush and intimately involved in Gerald Ford's campaign against Reagan in 1976, has also promoted his special assistant Dick Darmon, a protégé of Club of Rome member Elliot Richardson, to superstar status in the White House.