EIR Economics

The Saudis, the financial markets, and the oil price

by David Goldman

According to reports received by *EIR* from reliable sources, Saudi Arabia is making operational a contingency plan to regain control of the world oil markets and ensure the security of its regime. Additional reports erase all doubts that the contingency plan exists. The question which events are now beginning to answer is what version of the plan will go into effect, and how fast.

The plan, according to the most detailed account *EIR* has, includes:

1) an initial increase in Saudi oil output from the present 4 to 5 million barrels a day to 10 to 15 million barrels;

2) a posted price of $22.50 rather than the present crumbling price of $34;

3) a second reduction in the oil price (if necessary) to about $15 per barrel; and

4) shifts in the $180 billion Saudi portfolio of foreign investments to favor political allies such as France.

The prospect of independent Saudi action has introduced a degree of unpredictability into the world financial situation such that all players in the game—including the London-centered faction which believes that a new world central bank will emerge out of the ruins of the present monetary system—have been taken off guard. Additionally, the prospects for a "debtors' cartel," i.e., a negotiating front of a significant number of large developing-sector debtors, have been advanced, as the case of Venezuela, which is reported below, highlights.

First public recognition of the Saudi plan came in Swiss national television's evening news on Feb. 7. Then on Feb. 10, Reuters circulated an announcement from the Saudi government that it was about to lower its oil price by $4 per barrel. Official lowering of the price to $30 is now expected to occur following Feb. 12-13 consultations of the Persian Gulf Coordinating Council, which includes Kuwait, the Emirates, and Bahrain. Also on Feb. 10, bank trading departments reported that "a major central bank" was on the market selling off billions of dollars of commercial bank deposits, in order to purchase U.S. government Treasury bills. Such a "flight to quality" would be expected by Saudi Arabia under the conditions prescribed by the plan.

It is still too early to insist on any single strategy on the part of the Saudis; as the chairman of one of the Aramco companies put it mid-week in a not-for-quotation discussion, King Fahd probably has not made up his mind. The principal consideration, he added, is security. The Iranians, who have escalated their war with Iraq, are threatening military action against the Saudis should the Saudis attempt to cut them out of the oil markets. Under the British-authored scenario for breaking up OPEC, which went into effect end of January (see Special Report, *EIR*, Feb. 15,) a *gradual* oil price deterioration is intended to be accompanied by Saudi readiness to cut back their own output to Iran's 3 million per day level to maintain a price floor, and wreck Saudi control of OPEC. The Saudis have been posed with the prospect of liquidating reserves, cutting back major investment projects, and packing off foreign workers, all of which amounts to a powerful threat to their regime. If the Saudis instead were to seize the initiative, and *raise* output while quickly lowering

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the price, they stand as the most financially cushioned force within the OPEC cartel, relative to their bitter British-tied enemies, Iran and Libya, whose financial position would quickly crack.

One analyst close to the Bank of England argues that an Iranian military success in the present offensive against Iraq will compel the Saudis to escalate their moves on the oil market. The analyst commented that the density of reports concerning Saudi moves, including reports that Saudi production is already up to 5 million barrels per day from January's 4.5 million level, indicates that the "Saudis are keeping the big stick in evidence."

Other market analysts insist the Saudis would never dare a price war for fear of direct Iranian attack. However, France's role in the Persian Gulf, which includes on-the-ground security for the Saudi regime, a fleet presence in the Arabian Sea, and a rapid deployment force of demonstrated effectiveness, appears to take the edge off the Iranian military threat to Saudi Arabia. Early February, France sold $6 billion in arms to Iraq, financed by Riyadh.

Further, what the Saudis have to lose under slow strangulation is not in question. World oil consumption has fallen rapidly in the last two years. The oil majors as well as parts of the U.S. and British governments have openly written off the Persian Gulf as a source of American oil, an attitude whose implications have not gone unheard in Riyadh.

Iran has also not hesitated to provoke Saudi Arabia's patience. This week, Iran bombed French military installations in Iraq. A British correspondent on Mideast affairs told *EIR*, "there is no doubt there is a faction in Saudi Arabia which would welcome" French military support in knocking Iran out.

The BNOC strategy

Attempting to run the price drop, the British strategy had two stages:

First, a price reduction by $4 to $5 per barrel, putting enormous financial pressure on Mexico, Venezuela, Indonesia, and Nigeria. In the case of Mexico, the loss of about $3 billion in oil revenue would bring Mexican external finances to just within the trigger-point past which the country would be forced to declare a moratorium; Mexico would have to apply to the IMF to obtain more funds and, in return, would have to give the IMF more control over its public budget.

In the case of the other three major oil-producing debtors, each nation would have no choice but to "pre-emptively" apply for an International Monetary Fund program, accepting what an official of Morgan Guaranty Trust called "preventive medicine." The weakening of these four leading developing nations would, British financial sources estimated, permit the International Monetary Fund to ride herd at the crucial upcoming summit meeting of the Non-Aligned developing nations at New Delhi on March 7.

A second drop in the oil price, to $25 per barrel, by March or April, would then force a major crisis in the world banking system, the British calculated, in time to force the leaders of industrial nations meeting at Williamsburg May 28 to accept supranational controls over their economies.

The threats of independent Saudi action have kept the scenario computers working overtime. "The possibility of an uncontrolled slide in the oil price has put us in something of a dilemma," said an official of the British National Oil Corporation. "We have been told by Gulf Oil that if we do not lower the price of North Sea crude to $30 by Friday [Feb. 11], then they will cease all purchases of North Sea. But the effect of doing this might be to tip the situation over."

The financial consequences

A $25 per barrel oil price at present production levels, as *EIR* reported Feb. 15, implies a Saudi payments deficit of $22 billion and an OPEC deficit of $73 billion, a circumstance the world financial system could not withstand. The shift of OPEC surpluses from $120 billion in 1980, to less than zero in 1982 has "lowered the world savings rate," as one Federal Reserve official put it, and a shift into big deficits would cause a general drain of funds from the already hard-pressed Eurodollar market, as well as from the market for U.S. government securities itself. The same Fed official said, "$22 [a barrel of] oil means a world financial catastrophe, and anyone who doesn't understand that is an idiot. The Saudis would be dragging the world to the precipice in order to deal with Iran and Libya!"

However, the world financial system is *bankrupt in any case;* as Morgan Guaranty Trust's chief economist Rimmer de Vries told the *Journal of Commerce* Feb. 9, twenty-five nations with $200 billion in debt payments are currently in arrears, and an additional 15 nations with $80 billion in debt are likely to go into arrears shortly. In principal, Mexico, Nigeria, and other nations who stand to suffer from the collapse in oil prices have already reduced imports to the point of cancelling all major investment projects and drastically reducing home consumption. Their problem is not export revenues but (especially in the case of Mexico) that all export revenues must be applied to debt service; the only solution for them is a moratorium permitting them to revive imports of investment-related capital goods.

Anticipation of an oil price drop has already thrown a monkey wrech into negotiations for Mexico's $5 billion "jumbo" loan from private banks. When Mexican Finance Minister Jesús Silva Herzog left for his early-February tour of European capitals, $4.7 billion of the required $5 billion in credits had been subscribed; reports following his return home indicate that the commitments have shrunk to $4.6 billion. State Department and Federal Reserve officials continue to circulate assurances that the loan packages now under negotiation for both Mexico and Brazil will be available in time, but private bankers are less confidant.

In the meantime, oil-producing Venezuela has broken into the picture as the new Mexico. With foreign reserves

variously estimated at $7 to $9 billion or lower, the country was not until recently a candidate for financial problems; but flight capital in excess of $100 million per day—triggered in part by fears of the implications of an oil revenue decline—are depleting those reserves at a staggering pace.

At this rate of deterioration, Venezuela could be broke by May, perhaps earlier. Oil exports have sagged to almost 1.3 million barrels per day—the lowest level in three decades—because of the global collapse of industry and an unusually mild winter in the U.S. Northeast. Eight international banks have sued the Venezuelan government for default because of late payments by the Venezuelan Development Corporation, just as Finance Minister Arturo Sosa was preparing to visit New York and European banking capitals to try to renegotiate government-backed short-term debt. Venezuela fell short by about $1 billion the last time it sent a finance minister abroad on such a mission, and that was when the government only needed $2.7 billion. Sosa now wants to refinance the entire $8.7 billion coming due this year—$3.5 billion of it by the end of next month. Bankers argue that Sosa doesn't have a chance, unless he accepts a "pre-emptive IMF program."

Venezuela, the major Ibero-American nation closest to the United States historically, has become the focus of debate over the "debtors' cartel" proposal circulated in one form by Colombian President Belisario Betancur, and in slightly different form by *EIR* Contributing Editor Lyndon H. LaRouche, Jr. Recent headlines discussing variants of this proposal, including that of LaRouche, belie reports that the "debtors' cartel" has disappeared from the political map. On the contrary, the new elements of unpredictabiility in the situation have convinced many developing-nation leaders that they have no choice but to take initiative themselves.

A brief selection from the intensive media coverage during the past two weeks includes:

On Jan. 25, *El Mundo*, an afternoon daily published by Miguel Angel Capriles, published a front-page editorial calling for formation of a debtors' cartel and a three to five-year debt moratorium.

On Jan. 28, *El Mundo* and *Ultimas Noticias* published a press release on LaRouche's policy proposal to the summit conference of Non-Aligned nations to begin March 7 in New Delhi, in which LaRouche details the necessity of the debtors' cartel tactic. The item was *El Mundo*'s lead banner headline.

On Feb. 5, *EIR*'s Ibero-America Editor Dennis Small, was interviewed at length on Venezuelan national television on prospects for a debtors' cartel.

Sections of the developing world's leadership are slowly becoming convinced that a crisis cannot be delayed, and the prospects for an accelerated oil-price drop add to the argument. There may yet be hope that industrial nations' leaders will learn this before they are called upon to sign away sovereign power over national economic policy to the International Monetary Fund.

The IMF advances its a global dictatorship

by Kathy Burdman in Washington, D.C.

The Feb. 10-11 meeting of the Interim Committee of the International Monetary Fund significantly advanced the IMF's timetable to establish a Malthusian "new Bretton Woods" monetary system by focusing on bringing the mightiest sovereign nation of them all—the United States—under supranational IMF policy control. The major subject of the closed-door meeting was the need to place the United States itself under an IMF "surveillance" program and to establish stringent control over U.S. banking regulation. If these programs are carried out, the IMF, as has been proposed by New York Fed President Anthony Solomon, former Lazard Frères banker Felix Rohatyn, and the British government, will be turned into a true "world central bank."

Publicly, the Interim Committee acted to ratify "Phase I" of the IMF program, the expansion of IMF quotas and the General Agreement to Borrow (GAB), to give the IMF the financial resources (at world taxpayers' expense) to bail out the private British, Swiss, and U.S. banks of the offshore Eurodollar market. The Interim Committee's final communiqué called for a 47.5 percent increase in IMF quotas—some $33 billion—and a boost in the GAB from $7 billion to $19 billion. If, as expected, Saudi Arabia caves in to the IMF's design, and as Saudi Finance Minister at the meeting Aba Khail announced he will do, the Saudis are expected to lend the GAB an additional $2.5 billion, and to lend the IMF a further $3 billion in general funds. It all adds up, even on the surface, to a $50 billion expansion of the IMF. The quota agreement, originally due to come into effect at the end of 1985, will be rammed through world parliaments, IMF officials said, by the end of 1983.

"All in all, the total effect is a very large and rapid increase, indeed, in our total resources of the Fund," British Chancellor of the Exchequer and Interim Committee Chairman Sir Geoffrey Howe told the press.

The script for the Interim Committee meeting was written the previous weekend at an exclusive meeting of bankers and financial officials at Ditchley Park, near London. According to participants, the 50 top financiers in attendance agreed that the world banking system could only "squeeze through" if American interest rates were to fall, if the American economy were to recover quickly, and if the process of debt reschedulings now underway were to go smoothly. "It was agreed