Do the Soviets have the capability to bring down the Western banking system?

by David Goldman

To the extent that the Soviet military command has well profiled the present U.S. administration, it understands that the most devastating weakness in America's policy profile is not at the Defense Department but at the Treasury and the Federal Reserve Board. "If the President is re-elected, and we continue what we are doing, the United States will be in good shape militarily in three or four years. The problem is, the Soviets know this," said a White House adviser who believes that the Soviets may trigger a general banking and currency crisis.

In *EIR*'s last issue, we reported that the Soviets, as well as Britain's Lord Peter Carrington and his friends in the United States, believe that financial pressure may break the administration's resolve to proceed with competent defense programs, including a beam anti-missile defense system. We showed that this perspective is the content of the present wave of hysteria concerning the American budget deficit.

We now proceed to examine, in preliminary fashion, the evidence that the Soviets currently have the capability to trigger a general financial crisis, sufficient to break the federal budget—unless President Reagan uses his war-emergency powers (under the Defense Production Act and similar legislation) to seize control of the situation.

U.S. intelligence community sources now worry that the standard U.S. government estimates of Soviet financial capability—which show the bloc deep in red ink on balance—may have missed the picture entirely. Near the peak of strategic tension, the Soviets have come up with financial resources to play $1 billion in the foreign-exchange market per day, for days at a time, in several consecutive weeks. These events are incompatible with the Bank for International Settlements' data on Soviet external deposits, which show funds of only about $8 billion in the Western banking system. One senior U.S. intelligence official points out that Soviet withdrawal of deposits from weak-link institutions in the interbank market would be sufficient to trigger a general crisis.

Scott Pardee, former chief of the New York Federal Reserve Bank's foreign exchange desk, told a Philadelphia conference Dec. 5, "One of the concerns of foreign exchange dealers in the interbank market right now is the trading behavior of the Soviet Union's banking arm in London. Ask a trader why the dollar is up and he will answer, 'The Russians bought dollars today.' The Soviet Union of course needs dollars to buy grain and other things in the West, but I have to believe that its current mode of operation is politically inspired. The Soviets can be very unobtrusive in markets when they want to be, even when they have big amounts to do.

"The tactics the Russians use in calling a bank and buying $50 to $100 million dollars from him are sledgehammer blows to the market. The Russians were particularly active as a buyer of dollars after the Soviet Union walked out of the Geneva talks on intermediate range missiles. Traders can only guess why.

"Perhaps the Soviets want the dollar higher so that they can get more for the gas and oil they sell to the West to the extent they might be paid in dollars for these exports. . . . Perhaps they want the dollar higher so as to place greater pressure on the goverments of the LDCs which are struggling to solve their debt problems, perhaps igniting a revolution or two. This is the guess of most foreign exchange traders today.

"Perhaps they want the dollar higher so as to further embarrass our allies in W. Europe and Japan, as could be read into the Geneva walkout," the speech continued. Pardee elaborated to *EIR*:

"It's embarrassing to the governments of Europe to have their currencies declining against the dollar. They are already annoyed with the U.S. for not having provided leadership on international monetary questions. Domestic political pressures will develop against those governments."

The Soviets' *fondo*

What is not known, more than what is known, concerning Soviet finances suggests that the Soviets operate one of the largest of the world's major *fondi* (concentrated, usually family-based, investment holdings), and that this *fondo* has assets of approximately $50 billion. U.S. intelligence analysts who have tracked Soviet finances, and lost sight of perhaps $40 billion in the past dozen years, have not been able to document the deployment of Soviet funds in such a way as to provide evidence to the public record. But there are indications that U.S. intelligence is proceeding on this assumption—as the U.S. government operation against oil trader Marc Rich suggests. Rich, using inside information on such developments as the 1975 Shaba province invasion in Zaire, as well as Mideast political developments, earned roughly $700 million during the past decade, according to intelligence sources, who also cite his role in oil trade between the Soviet Union and South Africa. But Rich never accumulated a personal fortune of more than a few million. These sources believe that Rich was merely an employee of a much larger, Soviet-linked financial operation, suggesting that the U.S. government prosecution of Rich was motivated by strategic grounds, as well as excellent legal (tax-evasion) grounds.

CIA numbers show a 12-year discrepancy ("errors and omissions") of about $40 billion in the Soviets' favor. This is a lead, but only that, regarding what is involved. Since the BIS is the principal source concerning Soviet holdings of hard currency in Western banks, it must be assumed that the BIS is complicit (by omission or commission) in providing misleading data.

One indication of the scope of Soviet operations is the size of foreign-exchange operations conducted in November and December, as noted above. It is not likely that the Soviets have the bank credit to conduct such speculative transactions, according to well-informed Western European banking sources, especially since both U.S. and German banks have been under pressure to reduce such lines to the Russians.

More likely is that the Soviets are backing all such transactions with cash deposits. The implication is that such cash deposits required are in the order of $5 to $10 billion at a shot, and cumulatively several times that, judging from our reports of market activity. This runs against BIS reports that the Soviets have a handful of billions of dollars in Western bank accounts. Soviet foreign exchange operations have been sufficient to shift the dollar exchange rate several percentage points in either direction, and sufficient to trigger an "avalanche" factor if deployed all at once—as they were. (What denomination such deposits may have had originally is irrelevant. The Soviets may take dollars, borrow foreign currency against them, and then sell the foreign currency for dollars, or, they might deposit gold against foreign currency to sell for dollars).

Apart from the reports concerning Soviet foreign-exchange operations, there were widespread reports in the European press, confirmed by West German industry sources, that the East Germans had emerged as the largest speculative element on the London silver market. Add to this the fact that the Soviets have dominated the Western European oil market's price developments during the past year, up to and including the most recent decline in the price of Soviet Urals crude Dec. 12.

The standard CIA material ("U.S.S.R.: Hard Currency Trade and Payments," Joan Parpart Zoeter, Office of Soviet Analysis of CIA, February 1983) tallies the principal items of the Soviet 1981 balance of payments (see table).

The huge errors and omissions level reported in the last line draws attention to itself. According to the CIA's tables, the accumulated errors and omissions for the ten years 1972-81 add up to $25.9 billion in hard-currency outflows from the Soviet Union. The 1982 figure is $3 billion, and no estimate is yet available for 1983, although preliminary indications suggest that it will be significantly larger than the 1982 figure. The money that the CIA has lost track of is, therefore, in the range of $35 to $40 billion.

This figure may not necessarily reflect the actual level of discrepancy. To start with, it assumes that all the national trade figures between the Soviet Union and Western European countries (which in any case show wide divergences) are accurate. However, when a computer shipment to the Soviet Union may be recorded as an American sale to South Africa, and when Soviet sales of raw materials proceed through a network of firms like Marc Rich's in which secrecy is paramount, it is impossible to believe that the existing trade data provide anything more than the crudest possible indication of what the trade situation might be.

A further problem in the trade figures is East bloc third-country operations, including all plant-building and "devel-

Soviet Union's 1981 balance of payments
(in millions of U.S. dollars)

Current account balance	100
Trade balance	−4,000
Exports	23,778
Imports	27,778
Net interest	−1,300
Military exports to LDC's	4,200
Other invisibles and transfers	1,000
Capital account balance	3,240
Gross credits	6,300
Government backed	2,100
Commercial	4,200
Repayments	3,200
Government backed	2,000
Commercial	1,200
Net change in assets	140
Gold sales	2,700
Net errors and omissions	**−5,840**

opment" projects. At the Nov. 16 meeting of the Swiss-Soviet economic commission in Paris, the *Neue Zürcher Zeitung* reported on Nov. 18, "The Swiss delegation proposed again to the Soviets that they purchase consumer goods in Switzerland; [but] the Soviets showed themselves less interested in consumer goods than in technology and know-how; they proposed in this sense cooperation in major projects in the Third World, in which case Swiss enterprises could simultaneously function as anonymous participants and suppliers."

According to Jan Vanous at Wharton, this is the first time the Soviets have proposed this sort of operation, but various East bloc countries have already conducted such projects, buying a significant share of the relevant equipment in the West.

The CIA report comments on the discrepancies as follows:

> When all of the line items are added up and net financing received is taken into account, estimates of sources of hard currency differ substantially from known or estimated expenditures. This calculated residual ("errors and omissions") in most years implies a net hard currency outflow for the Soviets. Apart from the likelihood that estimating errors are substantial, the residual reflects the exclusion from the accounts (because of substantial information gaps) of the U.S.S.R.'s:
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> a) hard-currency asssistance to other communist countries,
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> b) hard currency trade with the other communist countries,
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> c) net credits granted to LDCs to finance Soviet sales of machinery and equipment, including military equipment,
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> d) net credits—mainly short term—provided to the developed West to finance sales of oil and other commodities, and
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> e) hard currency expenditures in support of communist parties' terrorist activities in the West.
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> In the case of hard currency assistance to Poland, such assistance may have totaled $300 million in 1980 and close to $1 billion in 1981. The U.S.S.R. incurred a $500-$600 million deficit in 1981 in its hard currency trade with Hungary, the only East European country which provides sufficient data to make such an estimate. Estimate drawings on Soviet hard currency credits for machinery and equipment (excluding military) sales to the LDCs averaged $500 million a year in 1976-81. LDC repayments to the U.S.S.R. averaged an estimated $225 million a year, yielding net credits of $275 million a year. The amount outstanding at any one time on credits for oil sold to the developed West—assuming 30-day terms—could have been as high as $1 billion in 1980-81, up from $800 million in 1979 if the same terms are assumed. If in 1981 soft world demand forced the U.S.S.R. to offer more favorable credit terms for oil, the amount outstanding could have been substantially higher.

That is substantially all that the CIA has to say. Apart from this speculation, Mrs. Zoeter's report concludes that the Soviets, given low raw-materials prices and falling crude oil prices, continue to face a hard-currency shortage.

However, there are other known sources of Soviet revenue which dwarf the reported sources of discrepancies:

1) $12 billion per year in (as of 1983) known revenues from Arab countries in the course of 1983, at least at an annual rate. $7 billion (equivalent of 600,000 barrels a day) is reported to be obtained by the Soviets through sale of oil bartered from Iraq, Iran, and Libya for oil, and probably at terms extremely favorable to the Soviets. An additional $5 billion was paid by the Saudis to the Soviets for the arming of Syria.

2) Gold sales in excess of estimates (which vary wildly). The CIA chose conservative estimates; an additional 100 to 200 tons or more may well be sold, especially through London, which gives no numbers at all on Soviet gold, or through Switzerland, which gives numbers that are probably phony.

3) International narcotics traffic (see *EIR*, Dec. 20, "How the Soviet Union Is Taking Control of Europe's 'Underground Economy.' "). What cut the Soviets may have in the net profits of the world narcotics traffic is not known.

The CIA's published list of possible deployment of funds leaves out one obvious possibility: that the Soviets are *investing* hard currency in Western front businesses, Swiss or other trust operations, i.e., operating their own *fondo*. In this case there would be no reason for their hard-currency position to show up in the bank numbers gathered by the BIS. The laundering of these funds could be accomplished through Soviet gold operations in Switzerland alone, some intelligence analysts suggest. Since the gross volume of Soviet gold trading is many times in excess of Soviet net sales, the difference could be transferred directly from a gold-trading account to a trust account at the same Swiss banks the Soviets deal with.

This is the standard means for concealing the "beneficial ownership" of capital, and the only one for concealing very large amounts. A shell is purchased which purchases a shell, into which appropriate revenues are fed for investment. Given the Soviets' dominance in gold, oil, and other raw materials trade, it is not unlikely that much of the trading apparatus as well as mining, shipping, refining, and other operations represent either Soviet ownership, or joint ventures with non-Soviet oligarchical interests. Allegations have been made publicly to this effect about Occidental Petroleum (created with money that Armand Hammer, in effect, brought out of Moscow), and there is a short list of European banking and trading houses under American suspicion.