No dollar collapse yet

Despite weakening, the real dollar turnaround will come only with more spectacular and dramatic events.

President Reagan, immediately after his re-election, faces a set of drastic economic disappointments up through year end, and the outbreak of a generalized financial crisis toward the end of the first quarter of 1985.

The dollar has already fallen off from its September peak of DM 3.17, to DM 2.95 at the Nov. 9 Frankfurt fixing, a fall of almost 8%. The drastic dollar turnaround of which the IMF warned in its September Annual Report has, however, not begun. This is likely to be associated with a precipitous fall of oil prices during the first quarter of 1985.

As reported last week, OPEC's three-day emergency pricing session prevented, as expected, a generalized price war, but did nothing to prevent a major collapse of prices early in 1985.

This will coincide with a renewed outbreak of the Ibero-American debt crisis, whose much-hailed "solution" has consisted of attempts to prevent the major debtors from exceeding 90-days arrears, and ignoring the arrearages when they unavoidably pile up.

For the moment, there are only storm signals, not storm.

Immediately after Mexico revealed it would be earning $1 billion less annually because it was cutting its oil exports in conjunction with OPEC, Bank of America and British banks reduced by $1.2 billion the credit lines for Pemex, the Mexican state oil company. The *Wall Street Journal* stresses that Mexico will thus be doubly short on dollars and will see government deficits break through ceilings set by the IMF, which will scare the bankers who have not yet finalized the vaunted debt-rescheduling package. The *Journal* says there is no way the bankers will make up Mexico's dollar shortfall by increasing new loans beyond the $1.7 billion scheduled for next year.

Therefore, Mexico will have to run down its painfully accumulated foreign reserves and will again be unable to defend the value of its currency.

"We could lose more from capital flight than we lose in oil sales if people don't see the right decisions being made."

The Federal Reserve-run Country Exposure Review Committee is, meanwhile, quietly sorting out which Argentine debt U.S. banks must declare "substandard." Argentine loans which are more than 30-days late on interest payments are affected, but the Fed has bent the rules to permit banks to count on their books as performing that portion of the Argentine debt not thirty days in arrears. However, by the beginning of next year, all the $8.5 billion owed to U.S. banks will not only be substandard, but subject to writeoffs.

The IMF directors will not approve Argentina's deal with the IMF, announced September 25, until a "critical mass" had been reached on private bankers' commitments of the estimated $5 billion in new loans Argentina needs to be able to pay 1985 interest. However, the banks won't commit themselves until Argentina has won IMF approval, and the IMF has had to reopen negotiations over wage policy, monetary growth, and inflation which have blown out the Sept. 25 agreement.

The bankers are also demanding that Alfonsín prove he will be able to stand up to growing internal social pressures for scrapping the austerity program the IMF imposed on Argentina.

There is also a stampede of regional bankers against lending Argentina additional money required to pay next year's interest. Claremont Economics Institution chairman John Rutledge is telling the 150 regional banks which he advises: "They're pouring money down a black hole when they lend money to Argentina. We're going to see them hauled back again and again, agreements rupturing, and good money be poured down after bad."

As for the Reagan administration, visiting U.S. Undersecretary of State Kenneth Dam has made it clear the U.S. government would not help out Argentina—even by muscling the bankers—until Argentina were given IMF approval.

These considerations bear directly on Federal Reserve policy and the dollar; until now, the Fed has not loosened policy in the sense of providing more credit to the system. On the contrary, the Fed, since September, has removed funds net from the banking system; however, the plunging U.S. economy has absorbed much less credit. Interest rates have fallen as a result.

At the point at which the Fed must loosen in order not to jiggle interest rates or accommodate credit demand, but to counteract panic in the banking system, the dollar will crash.