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# Currency chaos reigns; experts talk stability

by Marcia Merry

Within hours after top financial officials of the Group of Seven nations (U.S., Germany, Britain, France, Italy, Canada, and Japan) gathered Sept. 20 at an unprecedented meeting at the White House to hear President Bush speak about financial stability and a new monetary system, the world currency markets opened to chaos. British Prime Minister John Major, currently the head of the European Community, called for an emergency summit of the 12-nation EC on Oct. 16.

The day after the Sept. 20 French Maastricht referendum, currency markets saw a run on the French franc, the British pound, the U.S. dollar, the Spanish peseta, the Danish crown, the Greek drachma, the Portuguese escudo, and the Irish punt. These runs continued a free-for-all which first broke out with the run on the dollar Aug. 21, and carried over as a mass dumping of the British pound and Italian lira to the point that on Sept. 16, the latter were taken out of the Exchange Rate Mechanism (ERM) of the EC—the system intended to keep currencies within a band of values, pending a single currency of a future unified Europe.

On Sept. 21 and 22, the franc came under attack. On Sept. 22, German Chancellor Helmut Kohl and French President François Mitterrand held a hush-hush meeting in Paris. The next day, French officials boosted interest rates from 10.5% to 13% in an attempt to defend the franc. A rare joint German-French statement was issued, pledging support for the franc-mark exchange rate.

On Sept. 22, British officials, responding to domestic economic turmoil, lowered the interest rate for the pound by a full point, from 10% to 9%.

However, despite these and dozens of other maneuvers and statements to inspire confidence, prolong the ERM, and prop up the dollar, the ERM and the dollar bloc are blowing apart as the reality of the rotten economies behind the currencies come to the fore.

What is required are national emergency measures based on the interests of the physical economy, not on schemes to protect favored financial holdings. These measures might include exchange controls, investment incentives, penalties, and others of the type used in past crises. However, as of Sept. 24, only Spain had moved in this direction, placing requirements and penalties for prospective currency speculation, and introducing capital controls.

Instead, August and September were characterized by central bank interventions to attempt to prop up currencies, interest rate shifts, and massive speculation. An estimated $500-1,000 billion worth of currencies have been traded daily on world exchanges as speculators have gambled on profit-making off expected central bank currency buy-ups, to maintain pre-set parities in the ERM and shore up other currencies. Much of this speculation is conducted by the currency trading divisions of the major banks, e.g., Citicorp, looking to cash in on the chaos.

**The mark.** The deutschemark has been blamed by Anglo-American financial interests, supposedly because it holds its value relative to other currencies because of German "high interest rates." In reality, the 9.75% key German interest rate was not among the highest in Europe. When, after intense pressure from Washington and London, Kohl lowered the rate on Sept. 14 to 9.5%, the "calming" effect this was supposed to have lasted less than 12 hours. Then the run on the pound resumed, leading to its removal from the ERM on Sept. 16. The Bundesbank has expended an estimated DM 60 billion in recent interventions to maintain various ERM currencies. German financial officials have been attempting to tamp down inflation, while the money supply grows because of the need to integrate eastern Germany's economy. In July and August, German money supply grew at an annualized rate of 8.5-9%.

**The franc.** By Sept. 23, the French franc was falling very close to its ERM floor level of 3.4305 francs per mark. Massive joint French-German interventions brought it up to 3.4100 to the mark. The Bank of France is estimated to have expended 50 billion francs ($9.8 billion) in interventions.

**The pound.** On Sept. 16, the pound fell through the ERM floor rate, and officials removed it from the ERM; and on Sept. 24, interest rates were lowered. The pound has fallen more than 8% against the mark in recent days. In contrast, on Aug. 24, Chancellor of the Exchequer Norman Lamont staged a press briefing at dawn at the Treasury Department to declare there was "not a scintilla" of doubt that the pound's value would be supported.

**The lira.** The government devalued the currency 7% the week of Sept. 13, and removed the currency from the ERM. Though re-entry was set for after the Sept. 20 Maastricht vote, this becomes more unlikely day by day.

**The krona.** The Swedish government declared an overnight interbank lending rate of 500% Sept. 16, eventually reducing it to 50%, though capital flight continued. The other currencies of Scandinavia have felt the same whirlwind.

**The peseta.** It joined the ERM in April this year; on Sept. 17, it was devalued 5%. On Sept. 23, the Bank of Spain moved to deter speculators by requiring domestic banks to match loans to foreign investors by depositing an equal sum, interest free, with the central bank.

**The dollar.** The U.S. currency has lost 20% of its value relative to the mark over the past year.



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