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EIR Documentation

The global financial crisis unfolds, 1944-98

by Jonathan Tennenbaum

In last week's Feature, *"Financial Crisis: The End-Phase of a 30-Year Disease," Jonathan Tennenbaum analyzed the origins of the present crisis, which involve the entire financial and economic history of the post-World War II period: the failure to undertake large-scale infrastructure projects and capital goods transfer to developing nations following the death of President Franklin Roosevelt and the end of World War II; the assassination of President John Kennedy, and the ushering in of "post-industrial" policies with the Johnson administration, which ended investment in scientific and technological progress in the United States and other developed nations; and the official end of the Bretton Woods system on Aug. 15, 1971, when President Richard Nixon decoupled the dollar from gold, beginning a several-phase process of decoupling financial instruments from any rational connection to the physical economy. The following chronology outlines the most important points in that process, which has brought us to the point where failure to organize a "New Bretton Woods" system, will condemn the world to a new Dark Age.*

July 1-22, 1944: A conference of 44 countries at Bretton Woods, New Hampshire, sets up an institutional framework for monetary, financial, and trade relations for the postwar period. A system of relatively fixed currency parities is agreed upon, with the U.S. dollar, backed by a gold reserve, as the central currency for world trade. Agreements are made for creating the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (later called the "World Bank"), as instruments of the new world monetary system.

April 12, 1945: The untimely death of U.S. President Franklin Roosevelt cuts short his plans to dismantle the British, French, and Dutch colonial systems, and to launch an era of worldwide infrastructural and industrial development. The new President, Harry Truman, reverses the essential thrust of Roosevelt's policy for the postwar period, and cooperates with the British strategy to launch the "Cold War."

Dec. 27, 1945: The IMF goes into operation.

Oct. 23, 1947: The General Agreement on Tariffs and Trade (GATT) is founded.

1947-49: The first postwar recession, largely as a result President Truman's anti-development policies, hits the United States.

From the late 1940s into the late 1950s, and to a lesser extent into the early 1960s, relatively fixed parities are maintained between the main currencies of the Western industrial countries, including the U.S. dollar, British pound, French franc, Swedish crown, Italian lira, and (from 1948 on) also the German mark.

Early 1950s: A series of major bank mergers occurs among the New York banks, forming giant banking groups which dominate Wall Street in the postwar period. On account of their strong historical, institutional, and family ties to the City of London and the British financial oligarchy, these Wall Street financial interests represent the core of an "Anglo-American elite" within the United States, known also as the "Eastern Establishment." The Anglo-American financial interests, represented by the Wall Street banks, exercise a dominant influence on the policies of the U.S. Federal Reserve System.

1957-59: A new, deep postwar recession engulfs the United States.

1958: For the first time, the main Western European currencies become fully convertible into dollars, or gold.

1958-59: Lyndon LaRouche carries out a study of the U.S. and other industrial economies over the period 1946-58,

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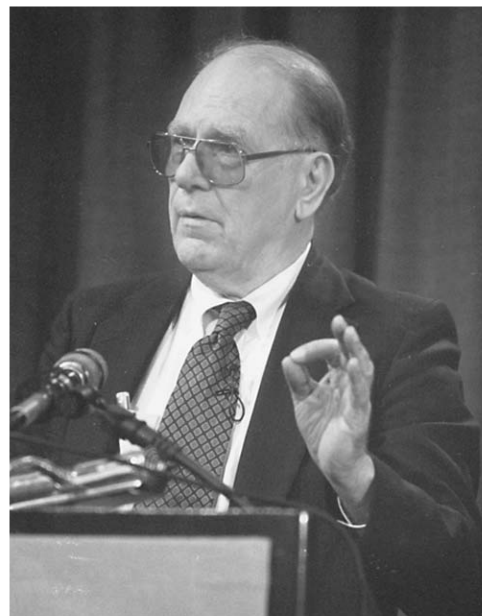


Delegates from 44 nations gathered outside the Mount Washington Hotel in New Hampshire in 1944 for the Bretton Woods International Monetary Conference. The demise of the Bretton Woods financial system, compounded by the disastrous effects of the "post-industrial society" ideology, have brought us to the brink of a collapse of the global monetary system. Lyndon H. LaRouche, Jr. (right) forecast these developments, and offers policy alternatives, starting with a call for a New Bretton Woods.

focussing particularly on the causes of the deep U.S. recession of 1957-58, which he identifies as "a turning-point in postwar history." LaRouche publicizes his conclusion, that unless prevailing economic policies were changed, a series of international monetary crises would occur during the second half of 1960s, leading to a breakdown of the Bretton Woods system of relatively fixed parities, and the long-term trend toward a new depression.

Jan. 20, 1961: John F. Kennedy becomes U.S. President. Kennedy's policies for stimulating technological innovation, particularly his aerospace development program and investment tax credit policy, sustain U.S. industrial growth into the mid-1960s. Parallel with this, strong industrial development continues in West Germany (the so-called German "economic miracle") and in France under President Charles de Gaulle.

Nov. 22, 1963: President Kennedy is assassinated in Dallas, Texas. Kennedy's pro-industrial policies are abandoned by his successor, Lyndon Johnson. New regulations are introduced concerning U.S. investment abroad, which provide the basis for a massive flow of dollars into Europe. Under the influence of U.S. Secretary of State George Ball and Bank of England Gov. Sir Siegmund Warburg, London becomes the main offshore center for a growing market of "Eurodollars" and "Eurobonds."

1967: The U.S. government under President Johnson take steps to cut back on the long-term U.S. space program, as part of a policy to further de-emphasize capital-intensive industrial development. At the same time, the increase in the U.S. budget deficit is accelerated by the high cost of financing the Vietnam War without new taxes. The total direct financial cost of U.S. participation in the Vietnam War is later estimated at $165 billion (1967 dollars).

In the course of 1967, the long-standing inflationary financial policies in the United States and Great Britain lead to a major crisis of the Bretton Woods system. The French central bank begins to exchange its reserves of dollars and pounds for gold. Jacques Rueff, the economic adviser to President de Gaulle, proposes a monetary reform which would include a 50% devaluation of the dollar and doubling the value of U.S. gold reserves. His policy is rejected.

November 1967: The British sterling crisis breaks out, leading to the first devaluation of the pound since 1949. The sterling crisis is followed by a severe crisis in the British automobile and other industries, leading to factory shutdowns and shrinkage of industrial employment. Great Britain becomes the first testing-ground for the "post-industrial society" policy. At the same time, West Germany and other Western European countries are hit by a major recession for the first time since the German "economic miracle" began.

March 1968: Due to panic sales of dollars for gold, the U.S. government orders closing down of London gold market for several days.

April-May 1968: France is hit by a major political crisis, brought on by student and worker strikes. Anglo-American banks dump their holdings in French francs, deliberately adding to the political destabilization which soon leads to the downfall of President de Gaulle.

April-June 1968: Assassinations of popular U.S. political leaders Martin Luther King, Jr. (April 4) and Sen. Robert Kennedy, brother of President Kennedy (June 5).

The loss of promising leaders, combined with the Vietnam War and the fear of nuclear weapons, greatly worsens the climate of "cultural pessimism" in the youth in Western countries. These conditions favor the spread of the so-called "rock-drug-sex counterculture" and the launching of the anti-industrial "radical environmentalist movements" among the younger generation, which are actively promoted by the Anglo-American establishment through its foundations and mass media. The 1968 student revolts become a kind of Western analogue to the "Great Cultural Revolution" in China, and create the political and cultural climate for a shift of capital away from productive activities, and into increasingly parasitical, speculative forms of investment.

By 1970, capital flight from the United States reaches $6.5 billion per year, growing to $20 billion in 1971. In Europe, there is panic dumping of dollars to buy gold. By August 1971, U.S. gold reserves fall to 25% of foreign obligations.

Aug. 15, 1971: President Richard Nixon suspends the convertibility of the U.S. dollar into gold, the first in a series of decisions which effectively put an end to the original Bretton Woods arrangements and open the way to "floating currencies."

December 1971: The "Smithsonian Agreement," among the United States, Japan, and West European countries, permits greater variation in the exchange rates among currencies. The U.S. dollar is devalued by 8%, and its rate is thereafter allowed to vary within +/–2.5%, compared to a maximum of 1% under the earlier Bretton Woods arrangements.

1971-73: Period of massive international currency and commodity speculation in the OECD countries.

Under the influence of U.S. Treasury Secretary George Shultz and others, "floating exchange rates" becomes official international policy, as affirmed by the 1972 Azores monetary conference and is further consolidated—despite warnings about the devastating consequences for the economies of developing nations and the world as a whole—at the Rambouillet Summit of 1975.

February 1973: The United States is forced to devalue the dollar by another 10% relative to gold. This does not stabilize the currency values, however. Between February and March 1973, the dollar falls by 40% against the German mark. In spring 1973, a dramatic collapse of the U.S. dollar causes currency markets to be closed for two weeks.

May 11-13, 1973: A secret meeting of the so-called Bilderberg Group at Saltsjöbaden in Sweden, including representatives of the London oil cartel and leading Anglo-American financial interests, makes plans for a 400% increase in oil prices and the recycling of oil revenues through the Anglo-American banking system.

October 1973: The "Yom Kippur War" in the Middle East, orchestrated with the help of the "pendulum diplomacy" of U.S. Secretary of State Henry Kissinger, leads to an oil blockade by the Organization of Petroleum Exporting Countries (OPEC) and, eventually, a fourfold increase in oil prices. Under "petrodollar recycling," secret arrangements are made to channel the increased flow of dollars from oil sales into the Anglo-American financial system. By 1974, some 70% of the oil income of the OPEC states (about $57 billion) is invested in foreign financial assets. About 60% of the money goes into U.S. and British banks and financial institutions. In 1975, a special OPEC meeting fixes the prevailing policy of accepting only dollars in payment for oil.

1974-76: The overall balance of payments deficit of (non-oil-producing) developing nations rises from $6 billion at the beginning of 1970, to more than $26 billion in 1974 and $42 billion in 1976. Oil money flows from the OPEC countries to Anglo-American banks, is, in turn, lent to developing countries to cover deficits due to their increased costs of imported oil. Actually, most of the money loaned to developing countries never arrives there, but is only transferred between accounts in London and New York banks.

By the end of 1975, developing countries' debt has rapidly grown to over $200 billion.

1975: G-7 economic summit in Rambouillet, France. Instead of carrying out urgent reforms of the world financial system, and eliminating the disastrous debt bubble, the participating governments agree to consolidate the system of "floating currencies" and encourage the further expansion of Third World debt.

1975: Deregulation of U.S. banking system eliminates privileged role of long-term investment credits, leading to a rapid expansion of the volume of bank credit flowing into sectors outside traditional industrial financing.

1975 is the last year the United States has a positive trade balance.

April 27, 1975: At a press conference in Bonn, Lyndon LaRouche puts forward his proposal for the reorganization of the world monetary system on a gold-reserve basis and the establishment of a new International Development Bank (IDB) to provide long-term, low-interest credit for large-scale transfer of technology and infrastructure projects in the developing countries.

Summer 1975: De facto insolvency of New York City, the largest city in the United States, which is subsequently placed under the financial dictatorship of a special state agency (the so-called Municipal Assistance Corp., or MAC). The financial collapse of New York City was made inevitable by the loss of tax revenues to the city, which in turn resulted from the collapse of industrial investment and growth of purely parasitical forms of employment. Instead of rebuilding the infrastructure and productive base of the city, a regime of austerity and looting is imposed by the so-called "Big MAC" plan to ensure debt payments.

Fall 1976: LaRouche's proposal for a debt moratorium for the developing countries, and establishment of a new inter-

national development bank, gain in influence among the member nations of the Non-Aligned Movement. These proposals are discussed at the Sri Lanka summit of the non-aligned nations in August 1976, and introduced into the debate at the United Nations General Assembly by the Foreign Minister of Guyana, Frederick Wills, on Sept. 27, 1976.

November 1976: Jimmy Carter is elected President of the United States. Carter had been handpicked in advance by David Rockefeller of Chase Manhattan Bank, and promoted internationally through the Trilateral Commission (including high-level individuals from government, finance, and corporations in the United States, Western Europe, and Japan), founded by David Rockefeller in July 1973. At an April 1975 meeting of Trilateral Commission in Tokyo, David Rockefeller had introduced Carter to leading international bankers and multinational company heads as "the next President of the United States." In attendance were key British figures, including Lord Roll of Ipsden; Lord Harlech (David Ormsby-Gore), head of Barklays Bank; George Baring; and John Loudon of Royal Dutch Shell.

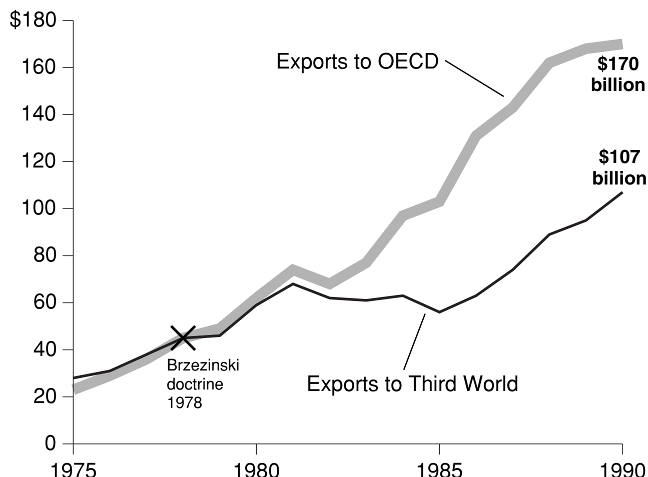
In the course of the following four years, the Carter administration implements a radical anti-industrial, anti-development policy both inside and outside the United States, dealing a heavy blow to the world economy as a whole. This includes: a disastrous increase in interest rates, ruining hundreds of thousands of U.S. farmers and industrial producers and drastically expanding the Third World "debt bubble"; deregulation of the U.S. financial system, as well as trucking and rail, greatly accelerating the trend toward non-productive, speculative modes of investment of financial capital; moves to destabilize Iran and other developing countries; strong measures to stop the peaceful use of nuclear energy throughout the world, and to implement a policy of "zero growth" along the lines proposed by Britain's Thomas Malthus in the 19th century and revived by the so-called Club of Rome beginning 1972.

July 31, 1977: Terrorist assassination of leading West German banker and industrialist Jürgen Ponto. Ponto, a close friend of German Chancellor Helmut Schmidt, was one of the chief promoters of the policy for developing the Third World using nuclear energy and other advanced technologies. Ponto was involved in European efforts to set up new monetary and credit institutions. Just weeks after Ponto's assassination, another prominent German industrial leader, the head of the West German Employers Union, Hanns-Martin Schleyer, is kidnapped by terrorists, and later killed.

1978: Michael Milken of the Wall Street investment company Drexel Burnham Lambert introduces "junk bonds" as instruments for speculative looting of U.S. industrial companies.

In the course of 1978, U.S. National Security Adviser Zbigniew Brzezinski repeatedly threatens Japan, demanding that Japan must stop large-scale technology transfers to developing nations. In the subsequent period, Japan's capital-goods exports to developing countries, which had been growing rapidly up to 1976-77, slow down and eventually even shrink in volume. At the same time, Japan shifts to the United States, Europe, and Australia as its main export markets (see **Figure 1**).

FIGURE 1
Japan's exports, by geographical area
(billions $)



Source: Japan Ministry of Finance.

June 1978: Under the leadership of Chancellor Helmut Schmidt and French President Valéry Giscard d'Estaing, Germany and France decide to launch a European Monetary System (EMS), with tightly linked exchange rates, supported by a European Monetary Fund in which participating countries place 20% of their gold and foreign currency reserves. The EMS policy emerges as a clear alternative to the monetary insanity of the Carter administration and the City of London. The British strongly oppose the EMS, and try to stop or delay its implementation. After these attempts fail, Britain eventually joins the EMS bloc.

September 1978: The political party of French President Giscard proposes a $100 billion development program for Europe and Africa.

As a counter to the French-German economic development thrust, the Carter administration, together with the British, launch operations to destabilize the Middle East.

October 1978: Breakdown of negotiations between British Petroleum and the Shah of Iran on renewal of the British-Iran 25-year oil agreement.

November 1978: President Carter appoints George Ball (co-founder of the Bilderberg Group, which had plotted the first "oil shock" in 1973) to head an "Iran Commission" in the U.S. government, as part of plans to oust the Shah of Iran and to lay the ground for a new "oil shock." In January 1979, the Shah is forced to flee Iran, and the Ayatollah Khomeini comes to power.

January-February 1979: "Second oil crisis" triggered by cutback in Iranian oil production. In the course of only six years, with the help of two orchestrated crises, oil prices have been increased 13 times!

March 13, 1979: Beginning of phase one of EMS.

May 1979: Margaret Thatcher wins election as Prime Minister in Great Britain, and pledges to "drive inflation out of the economy." At that time, inflation rate in Britain is 18% per year. The Thatcher government, with official adviser Milton Friedman, pioneers ultra-monetarist policies, radical "free-market" and "free trade" liberalization, globalization, privatization, and so on, which will dominate worldwide policy in the 1980s and 1990s.

In June 1979, British Treasury Secretary Sir Geoffrey Howe raises the British interest rates from 12% to 17%, causing an unprecedented "shock" to the British economy. After 18 months of the Thatcher government, unemployment in Britain doubles, from 1.5 million to 3 million.

September 1979: Sharp collapse of the U.S. dollar, as the Saudi Arabian central bank begins to sell U.S. Treasury bonds. Gold price reaches $400 per ounce.

Oct. 6 1979: Paul Volcker is named chairman of the U.S. Federal Reserve System. Volcker immediately announces a policy of dramatically increasing interest rates "to drive inflation out of the system." At this time, according to estimates of Morgan Guaranty Trust, some 500 billion U.S. dollars are circulating "offshore," outside the United States. The Eurodollar market comprises a significant percentage of total U.S. dollars. As a result of Volcker's actions, interest rates on the Eurodollar market go, within a few weeks, from 10% to 16%, and later even to 20%.

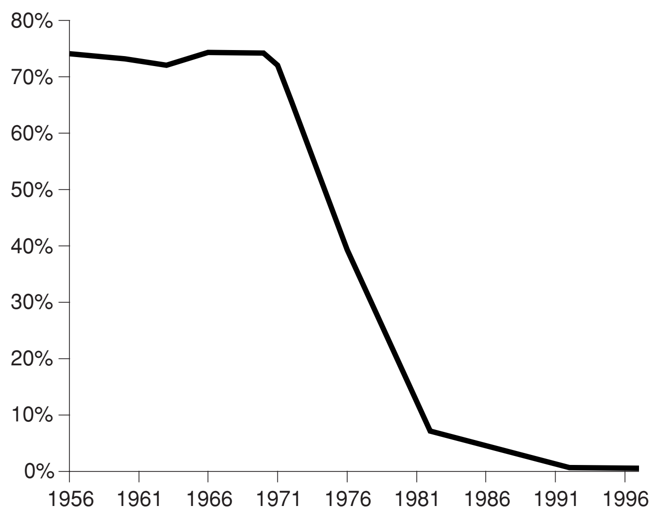
Oct. 16, 1979: Lyndon LaRouche releases the results of a computer-based analysis by his staff, forecasting a sharp collapse of U.S. industrial production, as a result of the Volcker measures. In an open letter to the U.S. Congress, on Oct. 29, LaRouche calls for the impeachment of Volcker. Unfortunately, no such action is taken. Subsequently, the LaRouche-Riemann econometric methods is uniquely accurate in forecasting and analyzing the disastrous effects of the Volcker high-interest policy.

March 1980: Carter signs "1980 Bank Deregulation and Monetary Control Act" into law. The interest rate ceiling for loans is lifted, effectively legalizing usury.

Largely as a result of "floating interest rates" on the Eurodollar market, and the policy of "rolling over" the debt by issuance of new loans, the debt of developing countries grows from less than $100 billion in 1970, to nearly $400 billion in 1979, and over $800 billion in 1982.

September 1980: Using the LaRouche-Riemann method of analysis of the economy's future capacity to produce, *EIR* forecasts a severe downturn in industrial production for 1981-82, because of the effect of Federal Reserve Chairman Volcker's policies. *EIR* is proven right, while all competing forecasts, including from Evans Econometrics, Data Resources Inc., Wharton Economic Forecast, and Chase Econometrics, prove to be wrong.

FIGURE 2
U.S. import-export trade as percentile of foreign exchange turnover



November 1980: Ronald Reagan wins the U.S. Presidential elections. The resounding defeat of Carter is largely an expression of protest in the U.S. population against the disastrous economic situation caused by the Carter administration policies. Unfortunately, the high-interest rate policy is maintained under the Reagan administration for two more years, until 1982, causing an unprecedented collapse of U.S. industrial production and a record wave of bankruptcies and takeovers of U.S. companies by foreign investors. In 1981, U.S. prime rate reaches over 21%, the highest interest rate since the Civil War (1861-65)! The policy of radical deregulation of the economy, borrowed from Great Britain's Thatcher, is pushed through, especially in the transport and financial sectors. In August 1981, Reagan puts through biggest tax cut in the postwar period, which greatly stimulates the flow of speculative and non-productive investments. At the same time, Reagan begins an attack on the trade unions. By 1982, the Teamsters union is forced to accept a wage freeze for three years, while other unions accept direct wage reductions.

In the course of 1981, world trade contracts by approximately 5%, for the first time since 1958.

Nov. 11, 1981: Poland cannot pay its debts, and applies to enter the IMF. This marks the beginning of a process of increasing IMF influence over the East European economies, eventually culminating in "shock therapy" in the former Soviet Union.

Late 1981-82: Outbreak of the Ibero-American debt crisis. As a result of the high-interest-rate policy, the debt of Ibero-America is more than $400 billion by 1982. Starting

late 1981, Anglo-American banks begin an attack against the Mexican peso. In February 1982, Mexican President José López Portillo makes a dramatic speech to the Mexican nation, accusing foreign interests of organizing the attack against peso and the huge capital flight out of Mexico.

Feb. 19, 1982: The Mexican peso is devalued 30% against the U.S. dollar.

April 1982: Thatcher launches military action against Argentina in the Malvinas War. Britain's revival of "gunboat diplomacy" (with help from U.S. Secretary of Defense Caspar Weinberger) is clearly aimed not only at Argentina, but is part of a campaign to pressure Ibero-American countries into paying their debts at all costs.

May 26, 1982: President López Portillo meets Lyndon LaRouche to discuss measures to save the Mexican economy. In August 1982, LaRouche publishes *Operation Juárez,* a proposal for formation of an Ibero-American Common Market and "debtor's alliance," which could survive an economic embargo and dictate terms to the creditor banks. At the same time, LaRouche repeats his call for a return to a gold reserve world monetary system and nationalization of the U.S. Federal Reserve.

August 1982: De facto default of Mexico on payment of foreign debt.

Sept. 1, 1982: President López Portillo announces measures for currency control and nationalization of banks, including the central bank, Banco de México. In a three-hour speech to the nation, López Portillo attacks "parasitical bankers" who are destroying the nation.

Oct. 1, 1982: President López Portillo addresses the United Nations General Assembly, sharply criticizing the high interest rates and collapse of raw materials prices, and warning against a "new Dark Age." Brazilian President João Baptista de Oliveira Figueiredo voices support for López Portillo at the UN.

Unfortunately, the Ibero-American countries are split and are forced, one by one, to back down to the creditors and the IMF. The result: The Mexican peso is devalued repeatedly, from 12 to the dollar in 1982, to 862:1 in 1986, to 2,300:1 in 1989, and finally, to 3,300:1 in 1993, when the "new peso" is introduced.

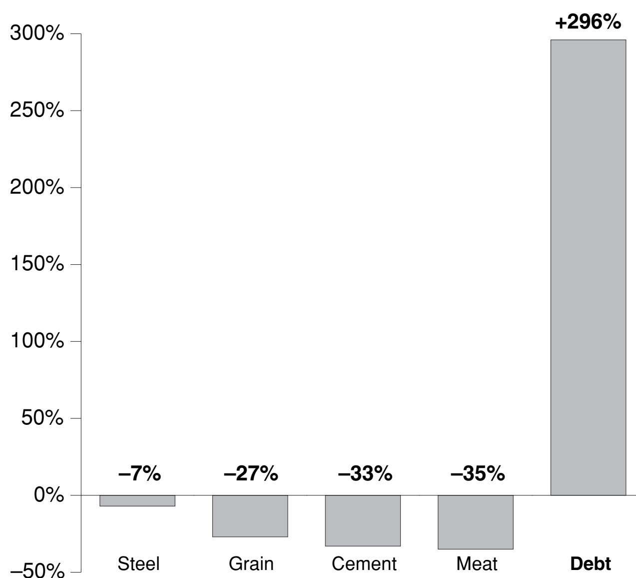
Between 1982 and 1987, total developing sector debt grows from $839 billion, to $1,300 billion (see, for example, the case of Argentina, **Figure 3**).

October 1982: U.S. Treasury Secretary Donald Regan lifts most restrictions on operations of U.S. savings and loan institutions, setting the stage for a period of "bubble growth" which leads to a major banking crisis in the second half of the 1980s. At the same time, the Reagan administration and the Federal Reserve pursue a policy of pumping enormous amounts of new liquidity into the U.S. financial system. This policy becomes known as the "Reagan recovery." By the end of 1982, the Fed has reduced interest rates seven times. Speculators can borrow money at low rates and invest it at much higher rates. New York Federal Reserve discount rates go from 12% in mid-1982, to 5.5% in August 1987.

FIGURE 3

Argentina: growth of foreign debt versus production, 1981-93

(percent change)



Sources: World Bank, ECLAC (United Nations), INDEC (Argentina).

1983: The United States becomes a net importer of capital for the first time since the Civil War. The U.S. budget deficit reaches $200 billion. Within the preceding six years, interest payments of the Federal government had more than doubled: in 1982, $52 billion; 1986, $142 billion, or 20% of the entire budget outlay.

1983: Panic run on Continental Illinois Bank signals onset of U.S. banking crisis. Government and private banks supply $11 billion in rescue funds.

During 1983, the productive sectors and living standards of Ibero-America are devastated as a result of the "conditionalities" imposed by the IMF. Mexico frees prices, and consumer prices increase 25% overnight; the Brazilian currency is devalued by 30%.

1984: For the first time, the United States has a negative balance in foreign investment. U.S. indebtedness on the capital market grows to $100 billion, twice that of the previous year.

August 1984: Renewed crisis of the Continental Illinois bank.

1985: The U.S. foreign investment balance reaches a negative $117 billion.

In the course of 1985, the banking system of the United States is hit by major failures. The S&L system in Ohio collapses, necessitating a three-day "bank holiday," and the U.S.

Farm Credit system defaults. The collapse of the U.S. S&Ls eventually wipes out an estimated total of $1,300 billion of assets.

1985: In a "reverse oil shock," OPEC prices fall from $26 per barrel in spring 1985, to below $10 at end of year, destroying smaller oil producers and causing a big shock to the economy of the Soviet Union, at this time the world's largest oil producer.

September 1985: At a meeting in New York's Plaza Hotel, the Group of Seven finance ministers agree to lower the value of the U.S. dollar against other currencies. The Plaza Accord triggers the biggest reversal on foreign exchange markets in the postwar period. Within a short time, the dollar falls by 30% against the yen and by 60% against the mark. Between 1985 and 1988, the value of the yen rose by 86% against the dollar, causing a major distortion of the Japanese economy. The Plaza Accord helped to accelerate Japan's plunge into the "bubble economy." Meanwhile, the U.S. trade deficit with Japan rose from a little more than $10 billion in 1980, to more than $55 billion in 1987.

October 1985: U.S. Treasury Secretary James Baker III convenes a meeting of representatives of the U.S. Federal Reserve and leading international banks in Washington, to discuss policy for "globalization." The World Bank and IMF are made into instruments of the globalization process, including promotion of liberal, new currency-convertibility rules, allowing foreign multinationals to quickly extract profits from national economies.

July 1986: Bankruptcy of the giant U.S. corporation LTV.

August 1986: Explosion of the Peru debt crisis, leading to sharp conflict between Peru's President Alan García and the IMF. The IMF declares Peru ineligible for loans.

Oct. 27, 1986: "Big Bang" deregulation of British stock market.

1987: The U.S. merchandise trade deficit reaches $187 billion, the biggest in U.S. history.

Feb. 20, 1987: Brazilian President José Sarney declares a debt moratorium, challenging the IMF. Unfortunately, under massive outside pressure, Brazil is soon forced to back down. On April 14, 1987, Brazilian Finance Minister Dilson Funaro, the architect of the debt moratorium, is forced to resign.

March 25, 1987: The dollar falls to an all-time low against the yen.

May 26, 1987: Lyndon LaRouche publishes a widely circulated press release entitled "Global Financial Crisis Predicted for October." His forecast is confirmed by subsequent events.

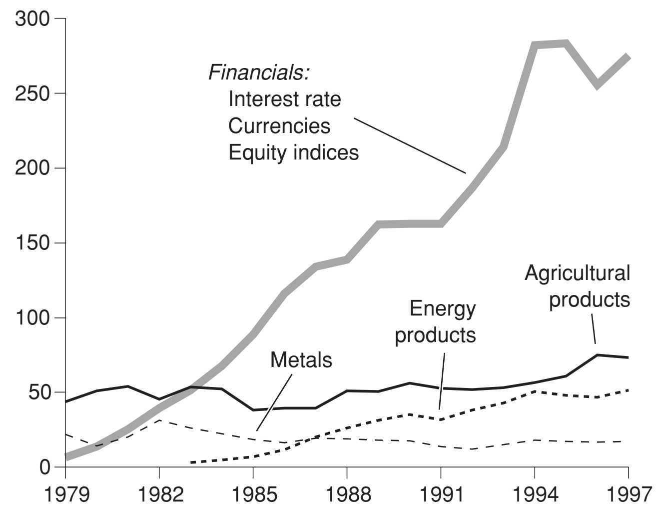
June 29, 1987: The big U.S. machinery company Allis-Chalmers goes bankrupt, part of a continuing process of disintegration of the U.S. industrial base.

July 14, 1987: Peru is hit by a massive capital flight, driving down the national currency. On July 28, President García announces exchange controls and nationalization of the banks, and declares that Peru will not spend more than 10% of its export income to pay the foreign debt. Eventually, however, Peru is forced to capitulate to the IMF.

FIGURE 4

Financials dominate futures markets

(millions of contracts traded)



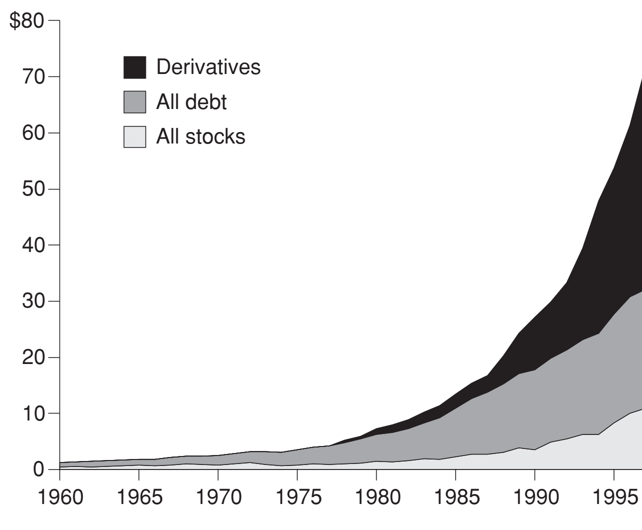
Oct. 19, 1987: On "Black Monday," the New York Dow Jones Industrial Average collapses by 508 points, the largest fall in history. Between Aug. 25 and Oct. 19, an estimated $1.5-2 trillion of financial assets are wiped out by the collapse of U.S. markets.

Subsequently, the Anglo-American financial establishment increases its pressure on Japan to pump money into the U.S. financial system. In the period following the October crash, the Japanese central bank continuously reduces its interest rates, encouraging money to flow into U.S. bonds and financial markets. This contributes significantly to holding the dollar stable through the 1988 U.S. election year. At the same time, the derivatives bubble begins to grow exponentially (**Figures 4** and **5**).

Oct. 12, 1988: At a press conference in Berlin, LaRouche forecasts the collapse of the Soviet Union and the imminent reunification of Germany. LaRouche calls for reunified Germany to play a central role in rebuilding the economies of the Eastern European nations. Later that year, LaRouche formulates the policy for building up high-speed rail "corridors" connecting East and West Europe, to make the industrially dense regions of Europe into the locomotive of a world economic recovery. This policy is circulated throughout the world in a series of documents and a book-length program entitled "The Productive Triangle: Paris-Berlin-Vienna" (1990).

March 17, 1988: Failure of the First Republic Bank of Texas, one of the largest banks in that state. The bank is

FIGURE 5
Hyperbolic growth of the U.S. financial aggregate
(trillions $)



temporarily saved by an injection of $1 billion from the U.S. Federal Deposit Insurance Corp. The rescue attempt fails, however. On July 1988, First Republic Bank becomes officially insolvent, leading to the largest bank liquidation in U.S. history.

Oct. 20, 1988: The largest corporate takeover in U.S. history marks a high point in the bubble of so-called "leveraged buy-outs" (LBOs) on Wall Street. The RJR-Nabisco LBO involves stock repurchases of $17 billion. Later, in 1989, the chain of debt created in connection with the RJR-Nabisco LBO scheme leads to the collapse of the LBO bubble.

November 1988: George Bush is elected U.S. President.

1989: According to Japan's Ministry of Finance, 70% of Japan's trade surplus worldwide is with the United States.

During 1989 and following, the collapse of the real estate markets in the United States accelerates. U.S. bank loans to real estate reaches $884 billion at the beginning of 1990, making up 25% of all bank assets. During the eight years of the Reagan administration, nearly $1 trillion flows into various forms of real estate speculation, and the total amount of private and public debt nearly triples, from $3.873 trillion, to nearly $10 trillion. At the same time, a construction industry study shows that the United States has a $3.3 trillion deficit in maintenance of basic infrastructure. Roughly 37 million Americans have no health insurance. Already in late 1989, the real estate market in the United States begins to collapse, leading to the savings and loans banking crisis of the early 1990s.

A survey by the IMF (published in 1990) warns about the dramatic increase in indebtedness in the U.S. economy. During 1953-80 the total debt—government, corporate, and personal—as a ratio of income, maintains a nearly constant level of $1.36 of debt per $1 of GNP. By March 31, 1989, the level had grown to $1.80 in debt per $1 GNP, greater than any U.S. debt level recorded in the 20th century, except for the Depression years of 1932-33. During the 1950s and 1960s, U.S. companies spent an average of 16% of pre-tax earnings on interest amortization. By the 1980s, this had increased to 56%.

March 10, 1989: U.S. Treasury Secretary Nicholas Brady announces a comprehensive plan for reorganization of Ibero-American debts. To support the debt-refinancing effort, Japan is pushed to put more money into the IMF, and is rewarded by upgraded status in the IMF and World Bank. As a condition for IMF guarantees on a new series of bonds and other debt-refinancing instruments, the Ibero-American nations are forced to carry out radical liberalization of their economies and financial systems. Mexico agrees to the "Brady Plan" in February 1990. Venezuela's President Carlos Andrés Pérez floats the national currency and lifts price controls, leading rapidly to a doubling of food prices.

April 7-11, 1989: GATT meetings in Geneva ratify a "market-oriented system of agricultural trade." In effect, the GATT policy increasingly undermines the basis for national food security, by preventing governments from using "protectionist measures" to support their domestic farm producers, and making nations increasingly dependent on food imports.

April 28, 1989: U.S. Special Trade Representative Carla Hills releases a report outlining a plan to impose massive pressure against trade partners using the so-called "Super 301" trading clause of the "Omnibus Trade and Competitiveness Act" passed by the U.S. Congress in 1988.

May 18, 1989: General strike in Venezuela against the IMF-dictated austerity policy of President Pérez.

September 1989: Harvard Prof. Jeffrey Sachs, a promoter of "shock therapy," becomes an adviser to Prime Minister Tadeusz Mazowiecki's government in Poland. One of the earliest measures is to eliminate food price subsidies, leading rapidly to a 500% price increase for many basic foods.

Sept. 13-15, 1989: The giant U.S.-Canadian retail sales corporation Campeau defaults on $450 million of interest payments, beginning a collapse of the $220 billion bubble of "junk bonds."

Oct. 13, 1989: Major crash on the New York stock market.

Nov. 9-10, 1989: Fall of Berlin Wall dividing East and West Germany. London sounds the alarm, warning against the economic power of a reunified Germany and the potential of an alliance between Germany and east European countries to rebuild the eastern European economies. British commentators warn against a revival of the economic theories of Friedrich List in Germany and eastern Europe—theories which they admit have proven superior to Adam Smith in the development of the industrial economies of Germany, the United

States, and Japan.

Nov. 29, 1989: Alfred Herrhausen, head of the largest German bank, Deutsche Bank, is assassinated, allegedly by terrorists. In the weeks before his death, Herrhausen had strongly criticized the destructive policies of the IMF and called for the establishment of special development banks for eastern European countries, on the model of the German state bank, Kreditanstalt für Wiederaufbau, which financed that nation's postwar reconstruction.

Jan. 1, 1990: Yugoslavian government submits to IMF "shock therapy" policy as proposed by Jeffrey Sachs: the Yugoslav currency is made freely convertible, credit issuance to the economy is cut, and price controls are eliminated, while salaries are frozen at the levels of November 1989. The price for reducing inflation is a 30% collapse of industrial production and mass unemployment. This economic disaster helped create the preconditions for the outbreak of the Yugoslav war in summer 1991.

Early 1990: Wave of failures and bankruptcies among big American financial institutions and transport corporations. These include the real estate giant Campeau (official bankruptcy on Jan. 18, 1990); the investment house Drexel Burnham Lambert, which had pioneered the speculative leveraged buy-outs (bankrupt Feb. 13, 1990); closing down of Greyhound Bus Co., Continental Airlines, TWA, and Pan American Airlines; Citibank and six other big banks in United States are technically bankrupt, but are kept afloat by the Federal Reserve, which continues to pump masses of money into the banking system.

March 13, 1990: Mikhail Gorbachov is named President of the U.S.S.R.

July 1, 1990: Currency union of East and West Germany. Under the terms of the union, the debts of state enterprises under the East German socialist system, which had an artificial character, are converted unchanged into "true" debts, which are taken over by Western banks at a fraction of their value. This results in a completely unnecessary debt burden on East German local governments and enterprises, many of which are bankrupted in the following years.

Under massive pressure from the British and French, and the Bush administration in the United States, the German government under Chancellor Helmut Kohl embraces radical neo-liberal economic policies toward eastern Europe. This includes applying a form of "shock therapy" to eastern Germany itself, in which, instead of modernizing and expanding industry, most of the industry is simply shut down. Between 1990 and 1993, industrial employment in eastern Germany is reduced by two-thirds. By the end of 1997, the official

Why financial bubbles must collapse

Among government officials, economists, and other leading professionals around the world, there is little disagreement concerning the existence of a gigantic speculative bubble on the world financial markets. However, in countless discussions on this topic the author and his colleagues have often been asked: "Why are you so sure that the bubble will collapse the whole system? Why couldn't it *just keep growing,* despite momentary setbacks, as it seems to have done for so long? After all, some famous experts consider that the remarkable performance of the U.S. economy in recent years, including the spectacular rise of the New York stock market, means that a fundamentally new type of economy has been created, a 'new economy,' characterized by permanent growth of financial markets."

This type of question shows that many people, among them professional economists, have not fully grasped the inseparable connection between the hyperbolic growth of financial assets on world financial markets, and a systematic destruction of the physical, productive base of the world economy, illustrated by Lyndon LaRouche's "Triple Curve" (**Figure 6**). In order to help remedy this gap in understanding, the author invented the following simple pedagogical device, in the form of a paradox:

Everyone knows that food production occurs in cycles of planting and harvesting. In the planting season, farmers must purchase seeds and various other kinds of supplies and equipment, which require relatively large expenditures that are only recovered after the harvest. Now suppose that the stock market and other financial markets in the country are rapidly growing, due to an inflow of funds from the outside (from foreign speculators, for example, or as a result of flight capital coming in from other countries whose economies are collapsing). Investing into the stock market promises a much, much greater rate of return, than the farmer could ever hope to obtain from agricultural production. (In fact, due to the collapse of farm prices, farmers in many places are actually losing money.) So, the farmer takes the money he would normally have used to buy seeds and other necessary supplies in the planting season, and invests it into the stock market instead. Now suppose *all* farmers do that. The flood of investment pushes the stock market to unprecedented levels, as the whole population pours their resources into the bubble. Unprecedented wealth is created—on paper. Unfortunately, when the harvest season comes, there is no food. Soon, nobody is alive to enjoy their stock market gains.

—Jonathan Tennenbaum

unemployment level has risen to more than 20%. Later, the unemployment wave spreads to West Germany.

July 7, 1990: G-7 summit in Houston agrees to place Soviet Union reform under IMF control.

Jan. 7, 1991: U.S. government takes control of a large bank in the northeast United States, the Bank of New England, after huge injections of government money fail to stabilize the bank.

Jan. 16-17, 1991: Beginning of the massive U.S.-led aerial bombardment of Iraq. The Gulf War is orchestrated mainly by the British, through the strong influence of Thatcher on Bush; although the military campaign is nominally directed against Saddam Hussein, the deeper, geostrategic aim is to contain Germany and destroy the perspective of a powerful economic development process in Eurasia.

April 1991: Karsten Rohweder, another key German industrial leader and promoter of industrial development in the East, is assassinated. Rohweder, the head of the state holding company in charge of reforming East German industry, is shot by a sniper through the window of his house. Rohweder had strongly opposed the radical "shock therapy" applied to enterprises in East Germany, and placed the highest priority on rebuilding and modernizing industry. Rohweder's successor, Breul, pushes forward a radical "free market privatization" policy, leading to the virtual de-industrialization of eastern Germany.

April 11, 1991: California officials take control of Executive Life Insurance Co., with liabilities of $49 billion. This is the largest insurance company failure in U.S. history.

August-September 1991: After the failed putsch of Aug. 19 against Gorbachov, the Soviet Union is dissolved. Russia, Ukraine, and other former Soviet republics declare their independence. Unfortunately, the governments of the newly independent states of the former U.S.S.R. subsequently agree to the conditions laid down at the IMF conference in Bangkok in mid-October 1991, which open the door to the disaster of "shock therapy" and make successful economic reform virtually impossible.

Late 1991: Huge layoffs by U.S. industrial corporations mark the acceleration of a process which comes to be known as "downsizing" (reducing labor force, concentrating only on the most profitable, not the most productive, operations) and "outsourcing" (transfer of production to foreign countries with cheap labor). Parallel with the downsizing process, the U.S. commodity trade deficit increases sharply, reaching $175 billion by 1995.

November 1991: Major collapse in the $60 billion U.S. market of securities based on credit card sales.

January 1992: In Russia, the lifting of price controls, as part of the Jeffrey Sachs-Yegor Gaidar "shock therapy" program, leads to enormous price increases in food and other basic commodities. During 1992, Russia and Ukraine are devastated by hyperinflation and capital flight. The so-called "criminal privatization" leads to a massive transfer of assets to a tiny, corrupt elite of super-rich "New Russians" and foreign interests.

Jan. 3, 1992: In testimony to the Banking Committee of the U.S. House of Representatives, the head of the Congressional General Accounting Office states: "Not since the 1930s has the banking sector been in such a serious condition as now."

February 1992: Major crisis of the insurance company Lloyds of London. Lloyds is forced to raise an additional $3.6 billion to cover financial losses.

February 1992: The Maastricht Treaty is signed for creating the European Currency Union. Far from constituting a positive alternative to the collapse of the world financial system, the Maastricht Treaty is based on radical monetarist doctrines, imposing a regime of drastic austerity and virtually eliminating national sovereignty in the economic domain. The Maastricht "conditionalities" are a new wave of mass unemployment in Europe.

March 22, 1992: Insolvency of Olympia & York, the largest real estate company in North America. On May 15, 1992, Olympia & York officially declares bankruptcy in the United States and Canada.

Sept. 16-20, 1992: The European Monetary System breaks down, under sharp attacks by speculators. Between June and December, European central banks spend DM 188 billion to defend currencies. The Italian lira and British pound are forced to break out of the EMS, and the French franc is also hit hard. A leading role in the attack against the EMS is played by the speculator George Soros, whose Quantum Fund is based in the offshore financial center of the Netherlands Antilles.

It is later revealed, that the attack against the lira, and its resulting devaluation by 30%, had been planned and prepared at a secret meeting on June 2, 1992 on the royal yacht of British Queen Elizabeth II as it was anchored off the coast of Italy. Participating in the meeting were high-level representatives of international finance, including S.G. Warburg Bank and Barings Bank, together with officials of the Italian Finance Ministry. Part of the goal of the operation, was to create favorable conditions for a large-scale privatization of Italian state industries. In October 1995, collaborators of Lyndon LaRouche in Italy submit a formal legal brief against Soros to Italian courts, charging that his huge profits in speculation against the lira and other currencies were based on illegal manipulation and exploitation of confidential information.

Spring 1993: Italy's second largest industrial group, Ferruzzi, collapses and is taken over by creditor banks. This is one of the largest corporate bankruptcies in history, and is linked to losses in derivatives trading. The president of the Ferruzzi group commits suicide.

June 1993: The chairman of the U.S. House Banking Committee, Rep. Henry Gonzalez (D-Tex.), calls for an official investigation of Soros. *EIR* presents information to the committee.

Fall 1993: Second phase of EMS crisis. The narrow band

of European Union currencies is broken again, under massive attack from speculators. The French central bank uses up nearly its entire reserves in the effort to defend the franc. European Commission (EC) President Jacques Delors sharply condemns the activities of "Anglo-Saxon currency speculators," and calls for currency controls. Meanwhile, western Europe is hit by mass unemployment.

Aug. 2, 1993: Nobel Prize-winning French economist Maurice Allais warns in an article in the daily paper *Libération:* "The entire West is now in a fundamentally unstable financial situation. Poorly considered decisions could bring the whole world into a collapse, compared to which the stock market crisis of 1987 will seem negligible, and which could be comparable to the Great Depression." Allais warns that "perverse effects of unrestricted currency exchanges are very much underestimated." Referring to the speculative attacks against the EMS, Allais writes: "In the immediate term, only European Community exchange controls would give us the means to temporarily deal with the situation. . . . In fact, no measure that would permit the speculators to succeed, and to enrich themselves, is acceptable. . . . The current attack against the EMS, the only coherent monetary organization in the world, is based on gigantic disinformation. It is animated, supported and orchestrated in an incredible way by financial interests, whose origin governments should investigate."

Aug. 12, 1993: In a French TV interview, Prime Minister Edouard Balladur condemns the speculative attacks against the EMS, saying, "We must reform our world monetary, financial, and credit system, and act to protect the prosperity of nations from purely speculative activities. This is an economic and moral duty of all civilized nations. There are, all over the world, a group of speculators who would like a situation in which all the currencies of the world would float as much as possible. . . . We cannot agree to have billions and billions [of dollars] change direction in a quarter of a second and threaten the prosperity of a country." In the ensuing period, a violent debate breaks out in Europe on the issue of currency controls. Unfortunately, no decisive action is taken.

September 1993: The Shadow Open Market Committee, an influential private group of U.S. economists, sharply criticizes the low-interest-rate policy of the U.S. Federal Reserve, pointing out that it is causing an enormous flood of money into an "asset price bubble" on the financial markets.

Sept. 13, 1993: Historic peace agreement reached between Israel's Yitzhak Rabin-Shimon Peres government and the Palestinians under Yasser Arafat. A crucial feature of the agreement, elaborated in an annex to the signed document, is the plan to engage in joint projects for economic development, including water and transport projects. Unfortunately, much of the promised financial support for economic development of Palestinian areas fails to materialize. The World Bank plays a very negative role in this context; while trying to control the flow of development aid into the region, the World Bank rejects the approach of large-scale infrastructure projects and agro-industrial development, and insists instead on developing tourism and financial centers. In an interview, Foreign Minister Peres complains about the World Bank's foot-dragging and bureaucratic delays: "The World Bank . . . is a cumbersome, slow-working body and it will take years before we see any aid." The delay and sabotage of infrastructure and other development projects greatly aggravates the social and political situation in the Palestinian areas, threatening to destroy the peace agreement. Two years later, Middle East peace is nearly doomed by the assassination of Prime Minister Rabin on Nov. 4, 1995.

Sept. 16, 1993: In a heated debate in the European Parliament, EC President Jacques Delors attacks currency speculation, stating, "I don't see why, on the international level, we should not be studying ways to limit capital movements." Delors raises the possibility of invoking special EC laws to protect against speculation and reintroduce some form of capital controls in Europe. Delors is angrily attacked by officials of the British Treasury, who reject any form of currency control.

September 1993: In a series of public statements, the chairman and leading board members of Deutsche Bank defend the expansion of the financial derivatives market, rejecting warnings that a dangerous bubble has been created. These statements reflect the profound change in policy in Deutsche Bank, which occurred following the assassination of its chairman, Alfred Herrhausen, in November 1989. Deutsche Bank quickly abandons the German tradition of long-term industry-oriented banking, and embraces the "British model," oriented toward purely financial gains. Meanwhile, European countries experience mass protests by farmers and industrial workers over the collapse of real incomes, including a demonstration of 120,000 construction workers in Berlin, a one-day general strike by 1 million workers in Italy, and a major strike wave in France.

Oct. 4, 1993: On the orders of Russian President Boris Yeltsin, troops of the Interior Ministry, using tanks and other heavy weapons, open fire on the Russian Parliament building, thereby ending weeks of disagreements between the President and the Parliament by force. Most of the Western press hails this event as a "victory for democracy," ignoring the fact that 1) the storming of the Parliament put an end to Russia's short experiment with parliamentary constitutional government, effectively giving the President absolute, dictatorial powers; 2) although political motives were involved on both sides, the opposition in the Parliament against the "shock therapy" also reflected the real economic disaster going on in the country. During the first six months of 1993, consumer prices in Russia increased by 344%, while industrial production dropped by 18%.

October 1993: House Banking Committee Chairman Rep. Henry Gonzalez holds hearings on the dangers of financial derivatives. An expert from *EIR* is invited to testify. Unfortunately, no significant action to limit derivatives is taken.

Oct. 29, 1993: A "White Book" on employment and eco-

nomic growth, prepared by the EC under Delors, is presented to the European heads of state. With unemployment in the European Community reaching 20 million, the White Book calls for large-scale projects in the field of infrastructure (especially transport and communications), as a means to provide additional employment and improve the efficiency of the European economy. Later, at the Pan-European Transport Conference on March 14-16, 1994, the Delors proposal is concretized to include a plan to accelerate and expand the construction of a European high-speed rail system. Echoing the LaRouche "Productive Triangle" proposal of 1988-90, the European transport ministers propose developing "infrastructure corridors" linking western Europe with eastern Europe to Moscow and beyond. Unfortunately, the realization of this plan is blocked by British opposition against the Delors plan, and especially against Delors's proposal to provide additional financing for the projects through new credit mechanisms involving the European Investment Bank and European Investment Fund.

November 1993-January 1994: French economist Maurice Allais publishes several articles in leading French newspapers, sharply criticizing the policies of radical "free trade," financial liberalization, and "globalization," promoted by the World Bank and IMF. "A gigantic accumulation of debt is eating away at the core of the world economy," Allais writes in France's newspaper *Le Figaro* on Nov. 29. "The pursuit of global liberalization of the exchange markets . . . [is] at minimum adventurous, and in reality very dangerous." Allais also publishes a devastating critique of the official World Bank-Organization for Economic Cooperation and Development (OECD) study on "Trade Liberalization: Global Economic Implications," which predicted beneficial effects of "globalization" to European and other economies. Allais characterizes the methodology of the study as "pseudo-scientific" and "totally erroneous." "The same men at the World Bank, OECD, and GATT who hold out the prospect of an increase in wealth of $213 billion per year [as a result of globalization] by the year 2002, remain absolutely silent about the financial flows amounting to an average $1.1 trillion per day, 40 times more than the amounts corresponding to trade payments. These financial flows totally destabilize foreign exchange markets and make it impossible to apply trade agreements in any reasonable way. The fact that experts from such leading institutions practice such disinformation, consciously or unconsciously, is unbelievable."

December 1993: World oil markets experience the most dramatic price drop since 1986.

Late December 1993: One of Germany's most famous companies, Metallgesellschaft (MG), suffers losses of more than $2 billion in the derivatives market. The losses were incurred by a New York subsidiary of MG in connection with speculative futures contracts in oil.

Dec. 30, 1993: In a sudden and unexpected move, the fourth largest bank in Spain, Banco Español de Crédito (Banesto), is taken over by the Spanish Central Bank. Economics Minister Pedro Solbes informs the Parliament that the emergency government takeover and reorganization of Banesto is necessary in order to prevent a crisis "of the entire banking sector." Spanish banking officials estimate that $3.5 billion in state assistance would be necessary to rescue the bank, which had been involved in high-risk speculation in derivatives. Banesto is partly controlled by the J.P. Morgan bank of New York.

During 1994, the Federal Reserve begins to raise interest rates, helping to trigger a new wave of financial crises. Going into spring 1994, a major collapse is striking the "emerging markets" in developing countries, particularly in Ibero-America.

Jan. 14, 1994: The second largest bank in Venezuela, Banco Latino, is closed down by the government in connection with huge losses in speculative operations.

March 1994: It is made known that the French state-owned bank Crédit Lyonnais will receive a guarantee of 40 billion French francs to cover bad loans, mostly in the real estate sector. Crédit Lyonnais played a leading role in building up a huge real estate "bubble" in France during the 1980s.

April 10-20 1994: The securities trading subsidiary of the Swedish state-owned bank Nordbanken suffers enormous losses in interest-rate futures speculation, amounting to more than twice its entire capital base.

Spring 1994: Since January 1994, stock market values collapse 30-50% in Ibero-America. Mexico and Venezuela are especially hard hit. Many other markets around the world experience hefty falls in stock prices.

May 12, 1994: Speaking to "EIR Talks," regarding turbulence on the global financial markets, Lyndon LaRouche comments that what Maurice Allais is saying about the financial bubble and the "casino" type of economy, is absolutely accurate, as far as he goes. "What Allais failed to address, and what must be dealt with more than anything . . . is something that the average person in the street does not wish to believe is what is about to occur. . . . What is inevitable is a *complete breakdown* of the entire IMF-dominated, Federal Reserve-dominated, global financial and monetary system. There is nothing that can be done to stop that system from collapsing, unless we shut it down earlier.

"When the breakdown comes . . . we're going to have to start from scratch and build a new monetary system, a new banking system, and a new credit system generally. The United States government has some experience with that, beginning with our first Federal government under George Washington, when we took a bankrupt United States, with a bankrupt credit system, virtually no banking system worth mentioning, no currency worth mentioning; and within a short time, under George Washington and Alexander Hamilton, we were on the way to being, relatively, the richest and most powerful nation on the planet. So we've done that before, we could do it again. . . .

"Once the citizen realizes that the ship *Titanic* is sinking, the citizen is going to start doing some intelligent thinking about lifeboats, instead of trying to get a better stateroom on the sinking ship."

June 24, 1994: LaRouche publishes his famous "Ninth Forecast" in *EIR* ("The Coming Disintegration of the Financial Markets"), warning that "the presently existing global financial and monetary system will disintegrate. . . . The collapse is inevitable because it could not be stopped now by anything, except a politically improbable decision by leading governments to put the relevant financial and monetary institutions into bankruptcy reorganization."

June 16, 1994: Germany is hit by a major financial scandal, involving losses estimated at $2 billion by the firm Balsam AG and the export financing company Procedo.

June 22, 1994: The London government bond market suffers the sharpest drop since 1914. Roland Leuschel, the chief economist of the Banque Bruxelles Lambert in Belgium, writes in the British *Daily Telegraph:* "The countdown to the crash has begun. . . . We are paying the price today for the creation, during the past two years, especially in the United States, of the biggest financial bubble in human history."

June 1994: Before retiring as president of the EC, Jacques Delors sharply criticizes "the brutal and purist neo-liberal ideology" which ignores "the idea of the public good." Delors condemns the opposition of the British, Dutch, and German finance ministers to large public infrastructure projects. Delors in turn is attacked by former London *Times* editor Lord William Rees-Mogg, who calls the Delors infrastructure plan "insane," and warns that it "would push up European interest rates and cause a panic in the European bond markets." Lord Rees-Mogg expresses the hope, that the radical environmentalist movement will mobilize to stop infrastructure projects.

June-July 1994: Extraordinary instability on the world financial markets, sparked by a sharp decrease in government bond prices in all major European and North American markets. In Venezuela, President Rafael Caldera announces emergency foreign exchange controls to defend Venezuela from financial collapse. On June 30, the Venezuelan government creates an Emergency Financial Council, through which "the state will assume operational control of the national financial system."

August 1994: Russia's biggest private investment firm, the MMM company, collapses, causing millions of small investors to lose money.

August 1994: After a few weeks of calm, instability breaks out again on the international financial markets, connected with new increases in interest rates.

Sept. 9, 1994: The prominent British politician and financial expert Denis Healy proposes to impose a tax on financial derivatives speculation, warning that derivatives speculation poses a "systemic risk" to the stability of the world financial system. Healy is denounced in the financial press.

Dec. 6, 1994: The official bankruptcy of the richest county in the United States, Orange County, California, occurs as a result of an estimated $3 billion in losses incurred when the local government invested in derivatives contracts. Prior to the sudden losses, Orange County had been hailed in the United States as a "model" for how to expand income by investing tax revenues into speculative financial markets.

Dec. 20, 1994: The Mexican financial crisis explodes with the catastrophic collapse of the Mexican peso and the immediate threat of a default on Mexico's foreign debt. During the second week of January 1995, the Mexican crisis spills over into all of Ibero-America, causing currency and stock markets to plunge, especially in Brazil, Argentina, and Chile.

Jan. 20, 1995: Roland Leuschel, at Banque Bruxelles Lambert, warns of new financial turmoil. The scale of speculation is so large, he writes, "that no central bank and no government can control it. . . . There are no miracles. Bubbles inevitably burst sooner or later."

Jan. 12, 1995: The U.S. government and Federal Reserve announce that they will make $40 billion in credit guarantees available to Mexico, to stabilize the nation's financial markets. Since Jan. 1, a total of $60 billion in "stand-by" credit facilities has been provided to Mexico. In spite of the unprecedented scale of financial assistance, Mexico nearly goes into default at the end of January 1995. The default is prevented only after the IMF puts up $17.8 billion of its own resources. Meanwhile, Asian financial markets suffer sharp declines.

On Feb. 2, IMF Managing Director Michel Camdessus says, "Mexico was in imminent danger of having to resort to exchange controls. Had that happened, it would have triggered a true world catastrophe." Camdessus warns that Mexico-like crises could occur in 10 other countries.

Feb. 25-26, 1995: The British bank Barings goes bankrupt, in spite of urgent efforts to save it by the Bank of England. The immediate cause of the Barings bankruptcy is losses of $1 billion in derivatives speculation.

April 18, 1995: In a press release, LaRouche warns that the financial and political system of Japan is being pushed toward the point of breakdown, by the refusal of the U.S. government to acknowledge the severity of the global financial crisis. He writes: "Although many economists, such as France's Maurice Allais, have warned of the danger inhering in the ballooning bubble of the derivatives speculation . . . I am the only known economist internationally who has accurately described the process of cancer-like inevitability of the ongoing systemic collapse of the international monetary and financial system as a whole."

May 1995: After more than a year of heavy losses, eventually forcing it to close down its trading in Eurobonds, the famous British bank S.G. Warburg is taken over by the Schweizer Bankverein of Switzerland.

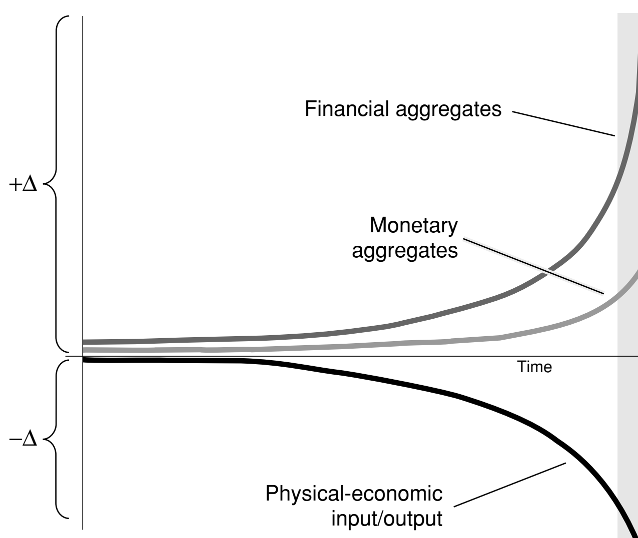
June 8, 1995: The Japanese Finance Ministry publicly admits that bad loans held by Japanese banks exceed $471 billion. The real figure of bad debts in Japan's banking system is estimated by leading international experts at more than $1

trillion. More and more signs point to a coming "meltdown" of Japan's financial system. Later it is revealed, that in the course of 1995, a secret agreement was made between the Japanese and U.S. governments, for the United States to provide up to $500 billion in emergency credit to stabilize the Japanese banking system, in case a chain-reaction of bank failures were to occur which might threaten the whole world financial system.

June 15, 1995: The Group of Seven economic summit in Halifax, Canada decides in favor of a policy of "reflationary crisis management," in an attempt to prop up the financial bubble at all costs. During July 1995, leading central banks begin to lower interests rates, and to pump new money into the financial system on an unprecedented scale. Japan plays a crucial role in this process. In accordance with the policy agreed in Halifax, the Japanese central bank lowers interest rates step by step, all the way down to 0.5%, flooding the international markets with cheap liquidity. This leads to a purely artificial growth of stock market values in Asia, Europe, and the United States—a phenomenon referred to by U.S. Federal Reserve Bank Chairman Alan Greenspan and others as "financial asset price inflation." At the same time, the international market of off-balance-sheet derivatives grows at an exponential rate.

December 1995: In articles and public speeches, LaRouche introduces his "triple curve," to explain the mechanism leading to the disintegration of the world financial system (**Figure 6**).

FIGURE 6
A typical collapse function



LaRouche's "triple curve" schematic shows how the hyperbolic growth of financial and monetary aggregates ("the bubble") proceeds at the expense of the physical economy, until a point of blowout is reached.

Aug. 21, 1995: Japan's second-largest credit union, the Kizu Shinyo Kumiai, goes bankrupt. Also, at the end of August, the Hyogo bank fails, in Japan's first bank failure in the postwar period. Growing anxiety about the private banks causes the Japanese population to withdraw enormous amounts of money out of the private banking system, and place it into the government-owned Postal Bank.

Many signs point to the fact, that high-level investors connected to British and other oligarchical interests, have begun to quietly pull money out of the stock markets and other financial markets, and to invest instead into precious metals and other "hard commodities." Anticipating a possible collapse of the entire financial system, these circles grab strategic raw materials, in order to have a controlling influence on the world economy in the future.

Feb. 8, 1996: The leading U.S. mouthpiece of the Anglo-American oligarchy, the New York Council on Foreign Relations (CFR), publishes an article hysterically denying the possibility of major financial crises. The article, published in the magazine *Foreign Affairs,* is entitled "Shockproof: The End of Financial Crisis." The author, CFR Director of Studies Ethan Kapstein, claims that "we have found a way to contain crises." "Over the past 20 years, the leading economic powers have created a regulatory structure that has permitted the financial markets to continue toward globalization without the threat of systemic collapse. . . . The financial difficulties of 1995 point to the strength, not the weakness, of the international regulatory structures." Kapstein's article is seen as a direct answer to the growing influence of LaRouche's analysis and policies.

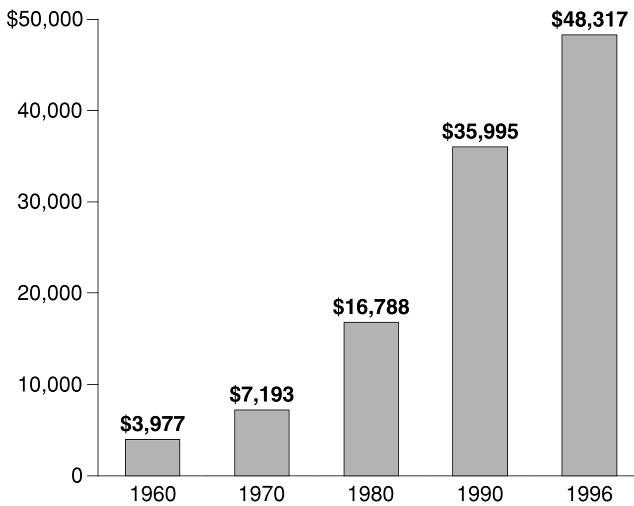
In 1996, the United States suffers the highest level of personal bankruptcies in its history, 1.125 million, or more than 1% of all households in the United States. This is four times the level of 1980. According to figures released by the Federal Reserve Board, the household debt of U.S. families reached $4.875 trillion by the end of 1996—an average of $48,317 per household, with an average yearly interest payment of $9,274 per year. This corresponds to a doubling of the ratio of debt to income for the average American worker since 1980 (**Figure 7**).

Meanwhile, a wave of giant bank mergers occurs during 1996: the merger of Mitsubishi and Bank of Tokyo ($648 billion), and Swiss Bank Corp. and Union Bank of Switzerland ($640 billion). And, there are major mergers in the U.S. banking system, including NationsBank ($290 billion) and First Union ($204 billion).

June 1996: The financial world is shaken by the announcement of huge derivatives trading losses by Japan's Sumitomo Corp., estimated at $2-4 billion.

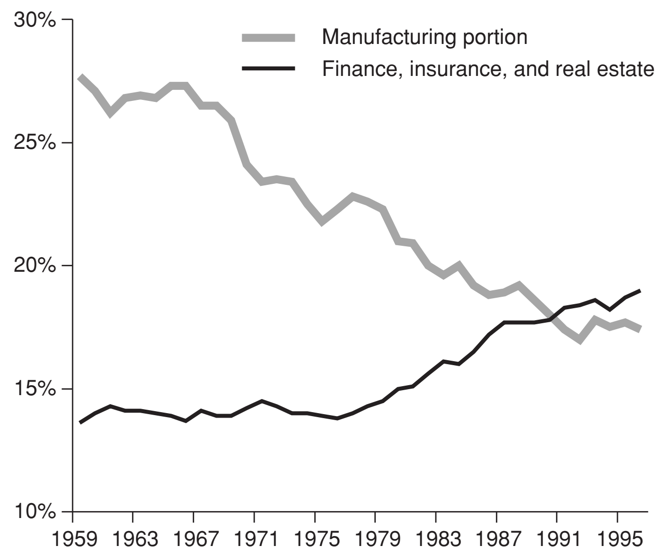
Feb. 15, 1997: At a conference in Washington entitled "Toward a New Bretton Woods," Helga Zepp-LaRouche and Ukrainian Member of Parliament Dr. Natalya Vitrenko issue a call to President Clinton to convene a New Bretton Woods

FIGURE 7
Household debt per U.S. household
(dollars)



Source: Federal Reserve Board, "Flow of Funds Accounts," "Household Table," various years.

FIGURE 8
GDP, by component: manufacturing vs. finance, insurance, and real estate



conference.

January-August 1997: The "asset price inflation" on the major stock markets reaches unprecedented levels. The New York Stock Exchange rises from 6,500 to more than 8,000 points in eight months. Over 40% of American families are investing in the stock market.

March 3, 1997: Thailand's largest financial company, Finance One PLC, goes bankrupt. The Thai government closes the stock market for one day.

March 9, 1997: In an article entitled "The $55 Trillion Horror Story," the London *Sunday Telegraph* warns about the danger of a total breakdown of the world financial system, which might be triggered by a collapse of the derivatives market.

May 14-15, 1997: International speculators attack Thailand's currency, the baht.

June 23, 1997: At a luncheon in New York, Japanese Prime Minister Ryutaro Hashimoto mentions the possibility that Japan might liquidate some of its holdings in U.S. Treasury bonds, estimated to have a total value of $450-500 billion. This statement, later denied, triggers a "mini-crash" on the New York Stock Exchange, the sharpest decline since the October 1987 crash.

Despite the growing instability of the financial markets, as revealed by repeated, sudden shocks, the rapid growth of the stock market bubble continues unabated. Between 1991 and mid-1997, the Dow Jones stock index more than doubles in value—a development having no basis in the real economy (see *Feature,* in this issue). During the first two quarters of 1997, stock markets in the western European countries, including France and Germany, increase by 20-30%.

June 27, 1997: Thailand suspends operation of 16 banks.

July 1997: Initial wave of collapse of currencies in Southeast Asia. Massive speculative attack against the Malaysian ringgit, the Philippines peso, and the Hong Kong dollar. At the same time, the Japanese banking crisis worsens rapidly. Emergency measures are needed to prevent the collapse of the Nippon Credit Bank, the Hokkaido Takushoko Bank, and other major banks.

Following the onset of currency and banking crises in Southeast Asia, the currencies of Poland and the Czech Republic also come under heavy speculative attack. Malaysian Prime Minister Mahathir bin Mohamad denounces the speculator George Soros, and calls for international measures to prevent the destruction of entire national economies by currency speculation.

August 1997: Simultaneous heavy losses on stock markets all over the world. On Aug. 15, the New York Dow Jones index falls by 247 points, and the London stock market experiences the biggest collapse since October 1987. The IMF announces a $17.2 billion rescue package for Thailand.

September 1997: The owner of the investment fund Berkshire Hathaway, billionaire Warren Buffett, announces that he is pulling his investments out of the stock market, and instead buying about $10 billion worth of "zero coupon" U.S. Treasury bonds. Buffett says he expects a new stock market crash.

September 1997: During high-level discussions in India

and China, Lyndon LaRouche's wife Helga Zepp-LaRouche briefs officials on her husband's forecast that a gigantic financial crisis is about to break out in Asia, that it will almost certainly erupt in October, and will change the entire world situation, and she presents an analysis of the causes.

Sept. 20, 1997: At the Hong Kong conference of the World Bank and IMF, Malaysian Prime Minister Mahathir condemns the "unjust and inequitable world order," and calls for controls against currency speculation. At the meeting, Japan proposes the establishment of an Asian Monetary Fund (AMF) to defend regional stability. U.S. Treasury Secretary Robert Rubin indicates his initial support for the idea, but the AMF proposal comes under strong criticism in the British financial press and elsewhere, especially on the grounds that it would challenge the authority of the IMF. The AMF is not realized.

October 1997: Full-scale explosion of Southeast Asia financial situation. Hong Kong stock market loses nearly one-quarter of its value in four days. Indonesia, threatened with a total financial collapse, calls for international help to rescue its currency. The IMF promises a $12 billion assistance package.

Oct. 14, 1997: Prof. Bruno Gehrig, a member of the board of directors of the Swiss National Bank, issues a strong warning about the danger of a global financial collapse. In a speech to the Swiss Bankers Association, Gehrig says, "Every day, far more than $1 trillion are being traded on the foreign exchange markets. . . . The failure of one participant, who is active in several currencies, can initiate simultaneous liquidity problems for his counterparts in other payments systems. The missing transactions could then block the payments of those counterparts to third parties within the payment system. Here is the danger of a chain reaction and a collapse of payments systems. . . . Settlement risks not only endanger the existence of individual banks, but pose a threat to the ability of the whole financial system to function. Most banks are completely unaware, that they are routinely being exposed to risks in foreign exchange trading, which are bigger in value than their transactions for several days. The amount of risk, even in respect to a single counterpart, can therefore exceed the base capital of the bank. . . . The systemic risks have reached an intolerable level."

Oct. 23, 1997: Hong Kong stock market crashes by more than 10% in one day. Simultaneous, sharp drops in stock prices throughout Europe, the United States, and Ibero-America.

Oct. 27-28, 1997: The New York Stock Exchange drops by 550 points in one day. Only massive interventions by the Federal Reserve, and multinational companies buying up their own stocks, succeeds in preventing uncontrollable panic and propping up the New York stock market.

Oct. 29, 1997: Historic visit of Chinese President Jiang Zemin to Washington. The international financial crisis is one of the topics discussed between Jiang Zemin and President Clinton.

Nov. 5, 1997: International conference in Bonn, Germany on creating a "New Bretton Woods System," organized by *EIR*. Speaking at the conference, Lyndon LaRouche emphasizes the fundamental, global nature of the financial crisis, which can only be overcome by radical reorganization of the world financial system. LaRouche points to the crucial role of cooperation between the United States and China, to carry out the necessary financial reform.

Nov. 17, 1997: Japanese government takes emergency measures to reorganize the bankrupt Hokkaido Takoshuko Bank, the tenth-largest bank in Japan. At the same time, the Japanese Finance Ministry announces the establishment of a special $62 billion fund (so-called Zaito fund) to rescue banks with liquidity crises. However, the total amount of bad debt in the Japanese banking system is estimated at $1-1.2 trillion.

Nov. 23, 1997: Bankruptcy of Yamaichi Securities, fourth-largest securities company in Japan. Yamaichi has liabilities of $53 trillion.

Dec. 3, 1997: The IMF announces a $57 billion rescue package for South Korea. As a condition for its assistance, the IMF imposes a so-called "stabilization program." Lyndon LaRouche denounces the IMF policy as "a medicine much worse than the disease." South Korea remains on the edge of a default, especially in connection with enormous amounts of short-term credits coming due.

Dec. 10, 1997: Since Sept. 30, the South Korean currency, the won, has fallen in value by 88%.

By the end of 1997, more than 5 million industrial jobs have been eliminated in Germany, 2.5 million of them in West Germany.

Jan. 12, 1998: Bankruptcy of Peregrine Investments in Hong Kong triggers a new, worldwide stock market collapse. The Japanese Prime Minister promises that the Japanese government will devote as much as $500 billion to stabilize the Japanese financial system, and to ensure that Japan would not be the trigger of a new "worldwide economic depression."

By February, it is obvious that the bailout package of the IMF has done nothing to solve the crisis. The disintegration of Japan's financial system worsens day by day. A second wave of crisis builds up from February into May. Beginning in February, LaRouche repeatedly warns that the explosion of the new crisis will include not only Japan and Southeast Asia, but also Russia and parts of South America, and will hit Europe and the United States "with terrifying force." LaRouche reiterates his urgent call for U.S. President Clinton to organize an emergency international conference, to declare the bankruptcy of the present world financial system and replace it with a "New Bretton Woods" system, based on the principles of physical economy. Tragically, the U.S. and other government failed to exploit the opportunity provided by the April 16 meeting of 22 nations in Washington, to initiate the process toward a New Bretton Woods. Indonesia was the first casualty. Who will be next?