U.S. Dollar Falls, No Sign of 'Recovery'

by Lothar Komp

Now it is, so to speak, official. The stockholders' hitherto anticipated upswing of the American economy, which Western government officials have talked about so much, has been misplaced or postponed once again. Despite 11 successive drops in interest rates over 18 months' time, no "recovery" is actually in sight.

The Bank for International Settlements (BIS)—the Swiss-based "central bank for central banks"—laconically confirmed in its current quarterly report on the situation in the international financial markets: "In the first months of 2002 the voices of enthusiasm which had been building up the financial markets in the fourth quarter, dispersed. From the beginning of the year until the first week of May the stock markets fell, along with long-term interest rates in the U.S.A., because their confidence in a strong economic upswing evaporated." The BIS also wrote meaningfully of a "sudden aversion with respect to companies that are strongly dependent on short-term debt." This category is large and growing.

After the discovery of more and more novel, sometimes also criminal methods for manipulating (reported) quarterly profits, and for camouflaging corporate indebtedness, the confidence in the "New Economy" has almost completely disintegrated.

Practically no one is taking even the high-gloss U.S. government statistics at face value at this point. This new attitude of investors was proven on May 28. Government and economic institutions went all-out, and in a few days produced three optimistic, high-sounding numbers. The consumer confidence level in May had climbed to the second-highest level since September of last year; sales of existing houses surprisingly climbed by 7% to the third-highest level of all time; and American consumer spending grew even further in April. The reaction of investors, however, was a further acceleration of the sell-off from the stock markets.

Flight into Gold and Swiss Francs

Simultaneously, a phase-shift took place on the foreign-exchange markets. In all the international financial crises since the mid-1990s, from Mexico to Russia, Thailand, South Korea, and Indonesia and over to Brazil, Argentina, Poland and Turkey, the dollar had continuously profitted as the currency of refuge. International capital flows, previously oriented in the direction of Asia, Ibero-America, or Eastern Europe, were steered around to the American financial markets. At the high point of the "New Economy" euphoria, the U.S. markets sucked up three-quarters of all worldwide balance of payments surpluses.

Now, the "safe haven" has proven itself a giant sinkhole of fraud and debt. If the balance sheets of the largest U.S. energy-trading corporations are about as trustworthy as the tax returns of mafia bosses, and if the share values of the leading technology venture firms can melt down even faster than the value of Indonesia's rupiah during the "Asia Crisis," there is little reason for an international investor to plunge savings into dollar-denominated values.

Already at the beginning of 2002, the net capital flows into the United States collapsed by around 75% compared to the previous year. According to one report by Lehman Brothers, foreigners' monthly purchases in 2000 and 2001 were on average $12 billion. This year such purchases plunged down to but $2 billion per month. The drying up of the capital in-flows did not fail to have an effect on the monetary system. On May 30, the euro climbed to more than 94¢ for the first time in 15 months, appreciating 8% in a month. The Japanese government has been intervening strenuously to prevent the yen from rising further against the dollar.

From the beginning of February to the end of May, the dollar fell by 8.4% compared to the Swiss franc; since the beginning of July 2001, it had lost 13.5%. On May 30 the Swiss National Bank took recourse to emergency measures. It dropped the discount interest rates on the gold market by two additional basis points to 0.99%, hoping to deter foreign investments. It is already rumored that the Swiss might, as had been done in the 1970s, impose capital controls, or even introduce negative punitive interest rates.

One further effect of the dollar crisis is the steady rise of the price of gold. On May 30 the price of a fine ounce in London shot to over $327, the highest level since October 1997. The Commonwealth Bank of Australia warned the day before that gold would become more dear by an additional $30 during June, should the United States continue its preparations for an attack on Iraq.

A long list of speculative funds and, not least, a few big banks such as J.P. Morgan Chase, Deutsche Bank, UBS, and Citigroup, are massively entangled in gold futures transactions, having for some time assumed a continuously falling gold price. A further increase of the price of gold could set loose a new "LTCM" catastrophe throughout the derivatives market.

In view of this, the breach in the dollar has only just begun. At the end of 2001, foreigners held $1.7 trillion in the U.S. stocks and an additional $3.2 trillion in government and corporate bonds. With a U.S. balance of trade deficit of $400-500 billion per year, untenable without maintaining the "New Economy" dogma, a persisting dollar weakness itself threatens to intensify the sell-off of dollar values. This will bring the global financial system again to the verge of breaking apart. This time the focal point of the disease no longer appears to be on the periphery, but in the center of the system.

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