Domestic Credit by Richard Freeman

The recovery plot

A second- or third-quarter downturn will become an unprepared President Reagan's biggest crisis.

The announcement on April 21 that durable goods orders rose merely 0.3 percent during March confirms that the previous month's big drop, first attributed to lower defense orders, represented the beginning of the end of the inventory accumulation blip. Indeed, the entire rise in estimated Gross National Product for the first quarter occurred in inventory accumulation, whereas final sales rose a scant 0.9 percent. Since retail sales were negative over the quarter, it is clear that the economy (stripped of inventory noise) remains on a mildly-falling trajectory.

Even Chase Econometrics's Lawrence Chimerine warned that the 1.1 percent rise in industrial output during March (according to the Fed index, which overstates the rate of change of output) simply means more inventory buildup.

At dealer level, auto stocks have risen to the three-month level, and auto assemblies fell during March in response. The same is true, as *EIR* has warned repeatedly, in the other consumer durables sectors which account for the nudge upwards from the economic trough.

Euphoria might not be so great had Fed Chairman Paul Volcker not thrown sufficient funds into the banking system to move banks from a net borrowed to a net free reserve position between the end of March and the middle of April.

As Merrill Lynch analyst Peter Canelo points out, the money supply rise for the week ended April 8 would have been reported at over $6 billion, rather than the $2 billion released by the Fed, except for some dubious tinkering with seasonal adjustments. Volcker is leaning heavily against the fundamental pressures for higher interest rates, using apparent statistical fraud to cover his tracks.

The most interesting question is, why so many individuals are compromising their credibility to blow air into the recovery balloon that had already begun to sag (in public perceptions) by the middle of March.

The "political" aspect is evident: the Reagan administration will stumble into an economic disaster by clutching at the recovery straw, Harriman-linked congressional leaders predict. The President, according to one well-placed congressional source, has "no international economic policy himself and no one to give him one. In the end, this will destroy Ronald Reagan."

Strange events at the Trilateral Commission meeting in Rome on April 19 provide a clearer explanation. According to Italian press accounts, the meeting "marked the beginning of the post-Reagan era." Two speeches in particular were significant. Robert McNamara argued that neither the banks nor the developing nations were responsible for the disastrous world debt crisis, but that the blame lay rather with Reagan and his excessive defense budget. The second speech was by Paul Volcker, damning the administration for opposing more intervention into the currency markets.

For the benefit of the credulous in Washington, Hobart Rowan reported the McNamara speech as an attack on the Felix Rohatyn-Peter Kenen variant of global refinancing plans, which the administration in any event opposes.

Meanwhile, Undersecretary of State W. Allen Wallis has formulated an American position for the Williamsburg summit that amounts to denying any world debt crisis exists, because the "recovery" will supposedly cure everything. Close associates of Wallis say he believes no such thing.

However, the *Wall Street Journal* is writing the same nonsense for the benefit of the President's breakfast-table reading. In a lead editorial April 20, it stated, "Most of the industrialized countries are well on their way to recovery, judging from the official indicators and ebullient stock markets world-wide. . . . [This] would pretty much solve whatever debt problem exists.

"That's not to say that some countries, and some banks, couldn't still go down the tubes. But the market has had ample time to discount the probability of this, and there's no reason it should lead to a panic. Poland has already declared a virtual moratorium on repayment of its debt, and that didn't lead to financial Armageddon, as some predicted. Anyway, there are established national procedures for dealing with potential bank failures."

A small group of Reagan administration advisers is warning, meanwhile, that a major debt crisis might break out as early as June, when most of the Third World convenes for the ministerial meeting of the United Nations Council on Trade and Development in Yugoslavia. However, according to one senior official, "The entire administration is logjammed on the issue, and Williamsburg will be a washout."