Volcker to Reagan: All deals are off

by Christopher White

As the dollar slid down to year lows against the major currencies of western Europe, Paul Volcker, Chairman of the Board of Governors of the Federal Reserve, signalled that he is now writing off all deals made with the Reagan administration over the period since 1982. The announcement was repeated in successive days of testimony before committees of the House of Representative and U.S. Senate July 18 and 19. The pretext was provided by the semi-annual presentation of the Federal Reserve's *Report on Monetary Policy* under the mandate of the so-called "Full Employment and Balanced Growth Act of 1978."

Volcker's remarks were supported by Preston Martin, another member of the Board of Governors of the Federal Reserve System, who has attracted attention in certain desperate circles in recent weeks, in seeming to disagree with Volcker's chosen monetary strategy.

International press coverage of the Volcker testimony, including from the *New York Times* and the *Washington Post,* focused on the chairman's remarks on the dollar and the budget deficit. The conclusion was drawn that Volcker opposes a fall of the dollar, because this will increase the cost of foreign financing for the U.S. government's deficit, and for the expanding trade deficit.

Thus, attention, as usual, was focused on Volcker's demand that the Congress cut the budget deficit.

Volcker identified six areas in which he said the economy is out of balance. The United States is, first, borrowing more than it saves; second, buying more from abroad than it is willing to sell; third, reconciling the discrepancy by piling up indebtedness; while fourth, trade partners dependent on U.S. export markets have continued high unemployment, and fifth industrial production has not matched consumption and employment, and sixth borrowers remain under strain or overextended.

These parameters of national bankruptcy, are known now to the professional economists as "lop-sided growth."

More substantially, Volcker reported, with his usual scant regard for the truth, after presenting his analysis of the disaster area he has, more than any other, made of the U.S. economy: "At their core, these major imbalances and disequilibria may lie outside the reach of monetary policy—or in some instances, U.S. policy generally. . . . The difficulty is that, as things now stand, some policy actions that might seem, on their face, to contribute toward easing one problem could aggravate others."

Later in the testimony he developed the point more concretely. "Our decisions with respect to providing reserves and reducing the discount rate have been influenced to some extent by a desire to curb excessive and ultimately unsustainable strength in the foreign exchange value of the dollar. But we have also had to recognize the clear limitations and risks in such an approach. The possibility at some point that sentiment toward the dollar could change adversely, with sharp repercussions in the exchange rate in a downward direction, poses the greatest potential threat to the progress we have made against inflation. Those risks would be compounded by excessive monetary and liquidity creation."

The same point was developed more succinctly by Preston Martin. "Although the Federal Reserve will continue to consider exchange rates and trade imbalances in its deliberations, we should not be looked to as a main source of a solution."

The architect of the policy given the name "controlled disintegration" in the mid 1970s, by the Council on Foreign Relations team that prepared, and then became, the administration of the hated Jimmy Carter, is here stating, before the U.S. Congress, that he is washing his hands of this policy of his own devising—in particular, the policy that has been in effect since the early fall of 1982, and was perceived, in the spring and summer of 1983, as the Great Recovery of so-called U.S. economic strength.

As is well known, the perception of "recovery" domestically, following in the wake of the rising dollar's genocidally extorted loot and tribute from the rest of the world, was what maintained the appearance of credibility for the lunatic and incompetent economic policies of the Reagan administration. In the process, the United States became a net debtor, dependant on foreign financing to cover internal expansion of indebtedness unsecured by domestic wealth creation, and to finance the, until now, ever expanding flow of imports that took the place of collapsed domestic production.

Now Volcker says, in effect, that he is handing control of policy over to those institutions which he made the nation's creditors. The arrangements by which the self-consoling illusions of the Reagan administration were maintained have been scrapped. The Federal Reserve's chairman is about to do to this President and adminstration what an earlier chairman did to the administration of Herbert Hoover.

Not surprisingly, Fidel Castro took the occasion of his recently concluded conference of Ibero-American trade unionists, on the subject of Ibero-America's debt, to praise the "heroism" of Volcker, who has single-handedly kept the United States going. Volcker's policy, the continuing legacy of the disastrous years of Jimmy Carter, and the evils of Milton Friedman, John Connally, George Schultz, and Volcker himself from the second Nixon administration, is after all, the best weapon the Russians have in their undeclared war against the West.

This was all projected by leading economist Lyndon LaRouche in his introduction to *EIR*'s *Quarterly Economic Report*, dated April 15, 1985. LaRouche reported in that location that as long as present policies were continued, the alternatives available were only two. Either a deflationary collapse of the bankrupt dollar credit system, or a hyperinflationary spiral. Efforts to avoid the consequences of the first would fuel impulses for the second, efforts to avoid the second would fuel the first. At that time, Volcker stated to representatives of this magazine, "I'm in the middle on that one." Volcker had been asked whether he supported Swiss-backed deflationary policies, or the Russian-favored hyper-inflationary alternative.

Shortly thereafter, political decisions, made in the wake of the bankruptcy of the privately insured Ohio savings and loans institutions, typified by the Bank for International Settlements' endorsement of an expanded international role for the European Monetary System's ECU, particularly with respect to the economies of Eastern Europe, made it clear that the deflationary alternative of rapid dollar collapse had been chosen. The existence of this Russian-approved variant set a limit on the dollar's upward movement. Since that point the dollar has collapsed more than 20% from its high levels of the early spring, and there is as yet no end in sight.

Volcker's testimony was buttressed by a chorus of experts from the economics profession, all of whom agreed with the line laid out by the chairman. These experts included Allen Sinai, Chief Economist of Shearson Lehman Brothers, Lawrence Chimerine, Chairman of Chase Econometrics and President of the Monetary Policy Forum, Nancy Teeters, a former member of the Board of Governors of the Federal Reserve System, and now Director of Economics at IBM Corporation.

The latter summarized a view put more circumspectly by all: "The result of combining these major exposures is a recession which could start as early as now."

On the other side of the Atlantic, the Volcker testimony was, for perhaps the first time, considered significant enough to be extensively excerpted by the *Financial Times* of London. The editors of that newspaper, in their adopted Orwellian version of the English language, agree with Mrs. Teeters and her friends. "About a year ago the economy lapsed from the rapidly expansionary phase of the cycle into a state which U.S. economists sometimes call 'growth recession'. . . . As a recent analysis by Morgan Stanley reminded us, on only one occasion out of the six growth recessions during the past thirty years, was the period of sluggish growth followed by a renewed burst of strong economic expansion. In all the other cases an outright recession, involving a fall in GNP and a significant rise in unemployment, followed, on average five quarters after the growth recession began." That is to say, "now."

How stupid then is the successor to Herbert Hoover at the Department of Commerce, Malcolm Baldrige. Baldrige has publicly asserted that the destruction of U.S. productive capacity, under present policies, is unimportant, for we are now a service economy. While Volcker was testifying, Baldrige was telling reporters in one of his quarterly press conferences, that the U.S. dollar should be devalued another 25% from where it is now, down to about 2.10 DM.

With this adopted perspective of "collapse now," the leaders of the financial institutions of the West have adopted for themselves the role of the Venetians during the siege of Constantinople in 1453. They are the ones who have opened the gates of the city to invite the Russian barbarians in to takeover, perhaps over the next few months.

They are ensuring that the momentum building behind the collapsing dollar, collapsing oil price, unravelling debt structures, and crumbling banks, like Bank of America and First Chicago, will become unstoppable. No longer will the Russians be the mere beneficiaries of the effects of Volcker's policies. They will be running the show directly. That is, as long as the ghost of Herbert Hoover continues to stalk through the White House.