

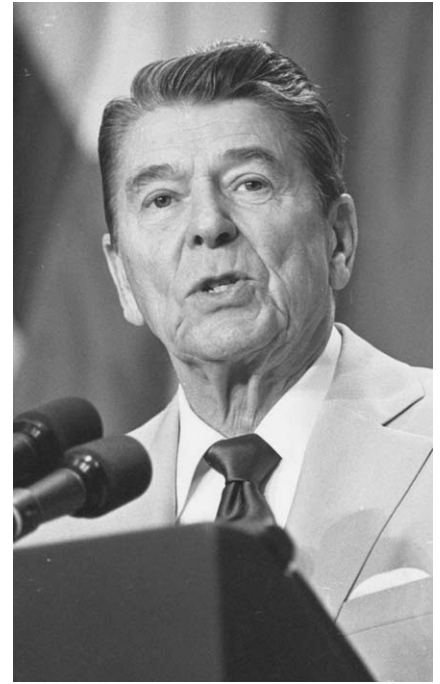
## Financial crisis: the end-phase of a 30-year disease

by Jonathan Tennenbaum

Following the outbreak of the full-scale Southeast Asian financial crisis in the fall of 1997, countless articles and reports have been written, analyzing the crisis and attempting to draw lessons for the future. Unfortunately, the vast majority of authors fail to acknowledge the most important fact concerning the Asian crisis: the fact, that the events in Southeast Asia are only part of an ongoing process of disintegration of the entire world financial system.

To understand the gigantic scale and deep causes of the global financial crisis, it is not sufficient to study the events of last few years. The origins of the present crisis go back over more than 30 years, and involve the entire financial and economic history of the post-World War II period. The history of the world financial crisis presents us with the picture of a disease which develops over a long time and generates more and more dramatic symptoms, before finally causing the death of the patient. In this case, the onset of the disease can be traced back to no later than the middle of the 1960s, when certain fundamental changes in Western economic policy were initiated, first in Britain, and then transmitted to the United States and other nations. The first generally recognized symptoms of this illness were the currency instability leading to the British sterling crisis of 1967 and the 1968 dollar crisis, and finally to the breakdown of the original Bretton Woods gold-reserve system in August 1971. The pathological process took hold more deeply during the course of the 1970s, leading to the Third World debt crisis and the emergence of a gigantic speculative bubble on the world financial markets during the 1980s. From the early 1990s on, with the aggressive globalization of the financial bubble and the rise of the so-called "derivatives market," the disease of the global financial system entered the "terminal stage," in which the system is absolutely doomed to destruction.

The crucial practical question for today is, not how to predict the exact moment and circumstances of the final collapse, but rather how to quickly establish a new world financial system, which can protect the world's population and nations from the effects of an otherwise uncontrolled disintegration of the old system, and pro-



*Left to right: Presidents Richard Nixon, Jimmy Carter, and Ronald Reagan, each of whose administrations made blunders in economic policy which have now brought us to the brink of a worldwide financial collapse.*

vide the basis for survival and real economic development in the future. This is the task of the “New Bretton Woods” policy initiated by Lyndon LaRouche. But governments will not be able to carry out the necessary actions of emergency bankruptcy reorganization of the present financial system, unless clarity has been established concerning the 30-year disease which has brought us to the point of its eminent collapse. Above all, the existence and nature of the disease itself, and the fundamental errors of policy which have permitted that disease to flourish and progress for so long, must be openly acknowledged.

Without a decisive break with the prevailing established trends of economic and related policy of the last 30 years, our world is doomed—as much doomed as a cancer patient who refuses to see a doctor, or the passengers and crew of the *Titanic*, who refused to acknowledge the fact that their ship was sinking and it was time to get off.

This article has the chief purpose, to provide conclusive, overwhelming documentation of the 30-year “global financial cancer” which has entered its terminal phase. We recommend that the article be read and re-read by anyone who still believes, that the crises in the Southeast Asian countries and in many other nations around the world are somehow isolated events, to be blamed on local conditions. Our historical overview should above all help readers appreciate the fact, that the present global crisis differs fundamentally from the crisis of the late 1920s and 1930s. What we are facing now, is much more than merely a new wave of stock market crashes, currency and banking crises worldwide. What we are facing can only be

compared to the fall of a great dynasty—a “dynasty” whose impending doom is symptomized by the cruelty, corruption, and criminal incompetence of the International Monetary Fund (IMF) and other leading institutions of the London-based world financial oligarchy. We are at the endpoint of a long historical cycle, at which awesome, “tectonic” forces, built up over decades and even centuries, are acting to bring down an entire set of ruling institutions and ruling ideas.

To identify the deeper cultural, political, and strategic nature of this historical “long cycle” in an adequate way, and to fully elaborate the fundamental principles, according to which a new world financial and economic order must be established in the immediate period ahead, lies beyond the scope of this article. For this, we refer readers to the writings of Lyndon H. LaRouche, Jr. We shall provide a few indications at certain crucial points in our account. This applies particularly to the United States, which naturally has played a central role in world financial and economic developments throughout the post-war period until today, and must therefore occupy a great deal of our attention in this historical review.

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## **The three phases of the post-war period**

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For the purposes of our analysis, it is useful to divide the post-World War II period into two main phases, with a short transition between them. First, is the phase of postwar recon-

struction and development (1945-63). There follows, from 1964 to 1966 a transition-period, during which a fundamental change in economic and social policies was initiated in the West. The third phase, from 1967 to the present, is the 30-year period of progressive degeneration of the global financial and economic system, leading to the present, acute breakdown crisis.

I shall now describe the first two periods in a summary way, before turning to a more detailed examination of the third period.

## **I. Postwar reconstruction and prosperous development (1945-63)**

The period from the end of World War II until the mid-1960s was characterized by relatively healthy, real physical growth in the economies of most nations of the world. This included the post-war economic reconstruction and recovery in Europe (particularly the European Community, including West Germany, France, and Italy) as well as Japan; strong industrial and technological development in the United States and the Soviet Union, and real economic development in many so-called “Third World” nations, including China, India, and many Ibero-American nations, which were able to build up a significant infrastructural and industrial base.

Generally speaking, although there was a growing competition and adversary relationship between the socialist and capitalist sectors of the world economy, both were oriented toward increasing the physical output of goods per capita, through capital-intensive forms of investment in agriculture, industry, and infrastructure.

This was a period of relative monetary stability under the 1944 Bretton Woods agreements and related arrangements. Those arrangements included relatively fixed currency parities, a central role of a U.S. dollar whose value was backed by a gold-reserve system, and relatively tight regulation of currency and banking systems. Trade agreements allowed for governments to foster and protect domestic producers by means of reasonable tariffs, subsidies, price-support measures, and supportive credit and tax policies, particularly in the area of food production and infrastructure, and in key industrial sectors. Generally, the government policies of the United States and other Western industrial nations discouraged speculation, and encouraged public and private investment into infrastructure, agriculture, and industry, with emphasis on high-technology capital goods production and improved scientific qualification of the population. Financial profits were mainly derived with the production and trade in physical goods. As a result, the financial system was strongly coupled with the real, physical economy.

However, the United States entered the post-war period with a problem: the premature death of President Franklin Roosevelt. Roosevelt’s policy for the world after the war, was to eliminate the British, Dutch, and French colonial systems, and initiate a period of worldwide industrial development in

cooperation with the Soviet Union, China, and other nations. After Roosevelt’s sudden death on April 12, 1945, his successor, Harry Truman, under the influence of Churchill and others, launched the Cold War. Instead of exploiting U.S. industrial capacity, which had been built up to a high level during the war, to help develop the post-war world, Truman’s economic measures unleashed the first of a series of post-war recessions in the United States in 1948-49. In 1954, Truman’s successor, Dwight Eisenhower, attempted to launch an economic recovery by means of a large expansion of credit. After a short-lived boom, however, this led to another, very serious recession, beginning 1957.

Around that time, Lyndon LaRouche, then working as an industrial consultant, made a careful analysis of developments in the U.S. economy, in interrelation with the other industrial economies in the period after the war, with special attention to the significance of the 1957 recession as a “turning point” in post-war economic history. LaRouche came to the conclusion, that unless the prevailing trends of economic policy were changed, the Western economies were heading toward a series of major international monetary crises, which he predicted would break out by the end of the 1960s.

LaRouche noted, among other things, that Eisenhower’s credit-expansion policy had led to an unhealthy “bubble” of consumer credit—especially connected with automobile sales—rather than stimulating investment in the capital goods sector as the basis for healthy long-term growth of the industrial economy. This error had been made on the advice of the head of the Federal Reserve System, Arthur Burns, who in turn was strongly influenced by the monetarist philosophies of Paul Volcker, George Shultz, and Milton Friedman. Under conditions of a structural stagnation of industrial development in the United States, Keynesian methods of stimulating the economy aggravated the shift toward short-term profits through a wasteful boom in consumer-goods and services and an unnecessary expansion of employment in administration and sales activities. This led to an increase in overhead costs per unit of physical output of the economy, without a corresponding increase in productivity through technological improvements in the industrial base. Thus, the expansion of credit was coupled with a decrease in the real, physical efficiency of the U.S. economy. Coming at the same time when industrial production in the Western European nations was rapidly expanding, the Federal Reserve policy was leading to a rapid depreciation of the dollar relative to the Western European currencies. This was inevitably leading toward a crisis of the Bretton Woods system.

LaRouche warned, that without correcting the fundamental errors of policy which had led to the 1957-59 recession, Western governments would respond to the next monetary crisis in exactly the wrong way, with disastrous consequences. LaRouche’s forecast turned out to be exactly right.

In the intervening period, however, a positive turn in U.S. economic policy was carried out under the administration



*President John F. Kennedy and Vice President Lyndon B. Johnson are shown a mock-up of the Gemini spacecraft in Houston, by astronaut "Gus" Grissom. Kennedy's promotion of the space program, among other policies, kept the United States on a path of modernization and technological innovation. But when Johnson came to power after Kennedy's assassination, the disastrous transition to the "post-industrial society" began.*

of President John Kennedy (from 1961 to 1963). Kennedy introduced a tax policy which greatly encouraged industrial enterprises to invest in new, advanced technologies, leading to higher productivity. This was coupled with Kennedy's expansion of the U.S. manned space program, and advanced science-linked military programs, using government investment to push forward rapid technological development and to expand and improve the education of scientists and engineers. These policies, together with the continued, capital-intensive industrial and technological development in Western Europe under German Chancellor Konrad Adenauer and French President Charles de Gaulle, ensured a relatively rapid rate of modernization and technological innovation throughout most of the Western industrial economies.

## **II. The transition period (1964-66)**

Unfortunately, Kennedy was assassinated on Nov. 22, 1963. Under his successor, Lyndon Johnson, together with the new Labour Party government of Harold Wilson in Britain, the previous policies of capital-intensive industrial development began to be abandoned. Tax, credit, trade, and monetary policies which had previously encouraged long-term investments into the productive sector of the economy and development of new technology, were eliminated, step by step. The new direction of policy was to create a gigantic expansion of consumer-goods and non-productive service sectors, offering higher rates of monetary return in the short and medium term. Although some positive effects of Kennedy's policies continued into the late '60s and beyond,

Kennedy's death marks a political turning point with decisive economic consequences.

It is important to understand the fundamental implications of this policy change, especially for the United States. Up to the beginning of the 1960s, it was generally taken for granted, that the foundation of America's prosperity, wealth, and power lay in the development of its industry, agriculture, and infrastructure. The rise of the United States to become the world's most powerful industrial economy, was based on methods of industrially oriented national economy, which were established by Alexander Hamilton, Mathew and Henry Carey, Friedrich List, and others during the nineteenth century. Those methods were strongly opposed to the "British System" of "free trade."

The traditional "American System" always favored a strong role of the state in promoting long-term productive investment in scientific and technological progress, sponsoring large-scale infrastructure development, promoting new branches of industry, and fostering domestic production by means of "protectionist" policies. It was commonly recognized in the United States, even up into the 1960s, that the principle of maximization of purely monetary profit by so-called "market forces," if permitted to govern economic processes without any interference or intervention from the government, would inevitably lead to the collapse of any industrial economy. To maintain a modern industrial economy based on scientific and technological progress, the state must play an active role: It must constantly intervene to maintain the long-term productive orientation of investment, to control

FIGURE 1

**Number of weekly paychecks required to buy new car in the U.S.**

(includes finance costs)

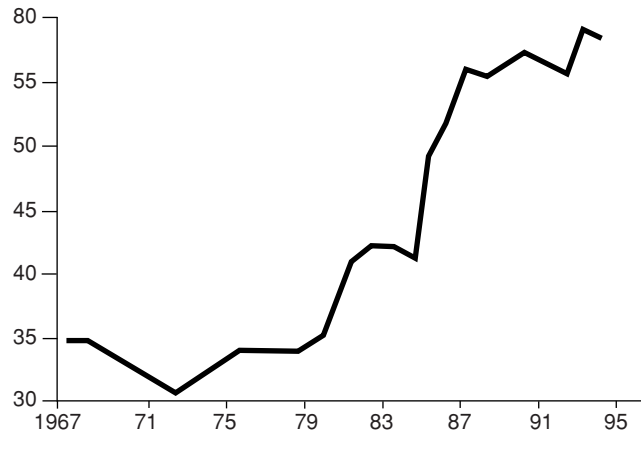
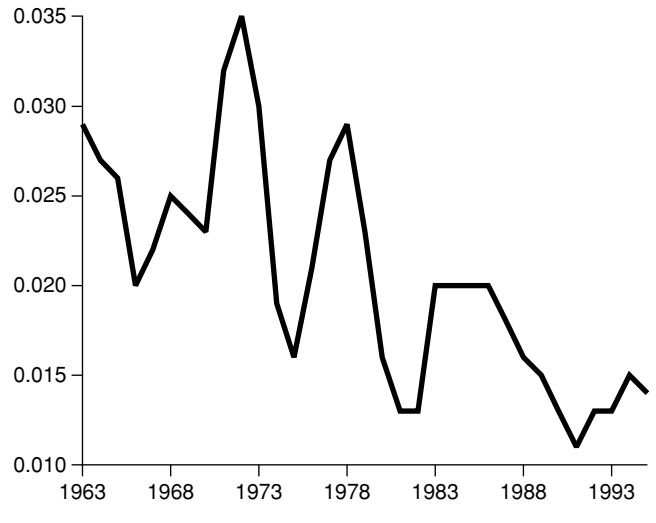


FIGURE 2

**Housing starts per U.S. household, 1963-95**



speculation and waste, and restrain the tendencies of the “market forces” for short-term profits at the expense of the long-term public interest. Similar principles of national economy were adopted in the industrial development of France, Germany, Italy, Japan, and other nations, and were key to the successful period of post-war reconstruction and development.

On this background, what began under Johnson and continued in later U.S. administrations, was a radical abandonment of the American System of industrial economy. This fundamental policy change is reflected in the concept of “consumer society” or “post-industrial society” which began to become popular in the mid-1960s. It is also directly connected with the launching of the youth counterculture, associated with rejection of traditional moral values, opposition to industrial technology, spread of rock music, “sexual liberation,” and growing use of marijuana and other psychotropic drugs. From Great Britain and the United States, these tendencies gradually spread to other Western industrial countries. As a result, the leading positive influence of the American System industrial model around the world, began to turn into its opposite.

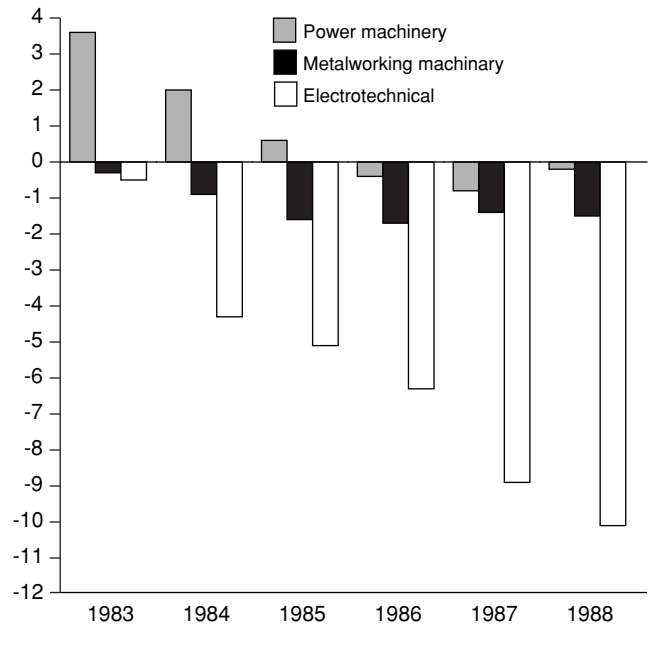
Many people consider, that since the United States has been the largest and most powerful economy in the world, and a military superpower, also, it must have the main responsibility for everything that has gone wrong with the world economy during recent decades. Although it is true that the spread of “financial cancer” is closely connected with U.S. economic and financial policies over the last 30 years, the standpoint of “blaming the United States” overlooks two important facts.

First, the traditional United States industrial system has

FIGURE 3

**U.S. net exports of capital goods (exports minus imports)**

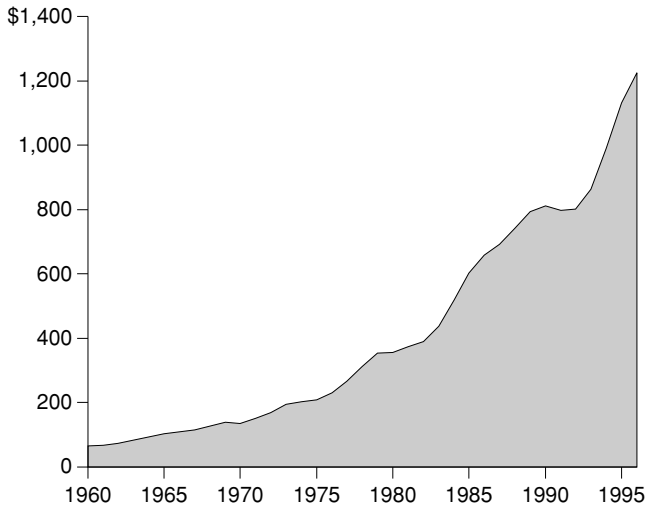
(billions \$)



itself been one of the biggest victims of the “financial cancer” of the last 30 years (see **Figures 1-3**). Contrary to myths which have been widely spread outside the United States, the productive base of the U.S. economy is vastly weaker today,

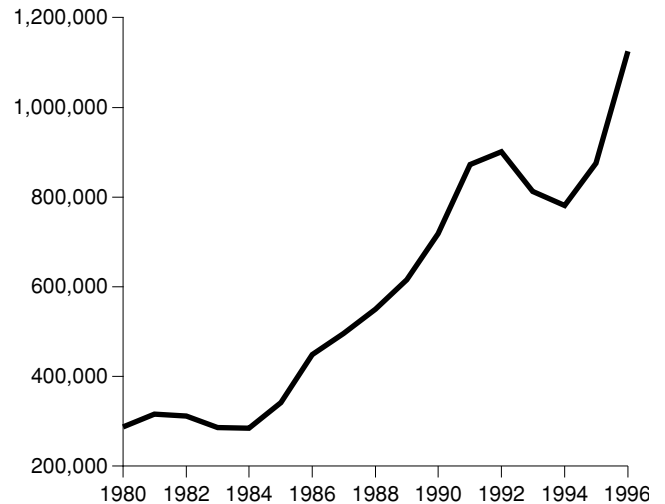
FIGURE 4  
**U.S. consumer credit, 1960-96**

(billions \$)



Source: Board of Governors of the Federal Reserve System, "Flow of Funds Accounts of the United States," "Household Table," various years.

FIGURE 5  
**U.S. personal bankruptcy filings, 1980-96**



Source: Administrative Office of the U.S. Courts, "Annual Report of the Director."

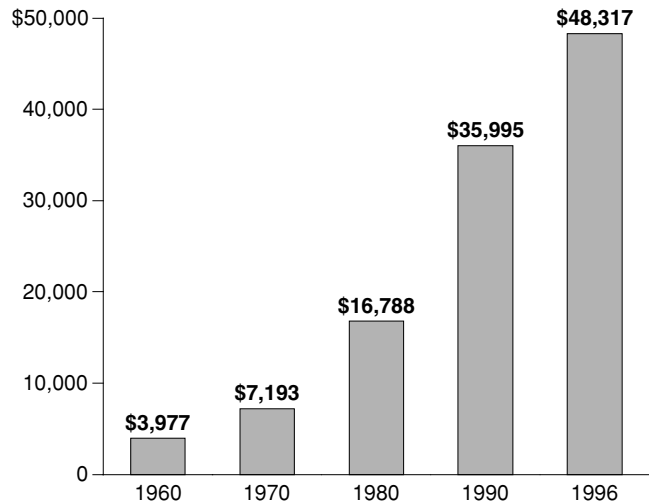
and the real, material living standard, and educational and cultural levels of the majority of the U.S. population is much lower, than in the middle of the 1960s. The impression of an economic boom connected with the "Information Society" distracts attention from the fact, that the U.S. economy no longer can support itself in physical terms, but depends on enormous imports of industrial equipment, semi-finished goods, and consumer products from abroad. Even so-called domestically produced goods incorporate a large and growing content which is produced outside the United States—often concealed in the operations of multinational companies. At the same time, the official U.S. trade deficit in physical goods was more than \$198 billion in 1997.

What has happened, is that a shrinkage and decay of the real productive base of the U.S. economy is being compensated for by artificial purchasing power coming from the financial "bubble." This process cannot be maintained indefinitely. Already in 1997, more than 1 million U.S. households officially declared bankruptcy, largely because of the decline in real family incomes (despite an increasing number of jobs) and the pressure of a huge accumulation of consumer debt. (See **Figures 4-7.**)

Second, a careful study of the broader historical background proves beyond any doubt, that the policies which have ultimately been responsible for the "global financial cancer," did not originally come from the United States. Those policies are much older; they originate in the British Empire, and were imposed upon the United States, almost like a colony—by the Anglo-American financial oligarchy, through what is

FIGURE 6  
**Household debt per U.S. household**

(dollars)



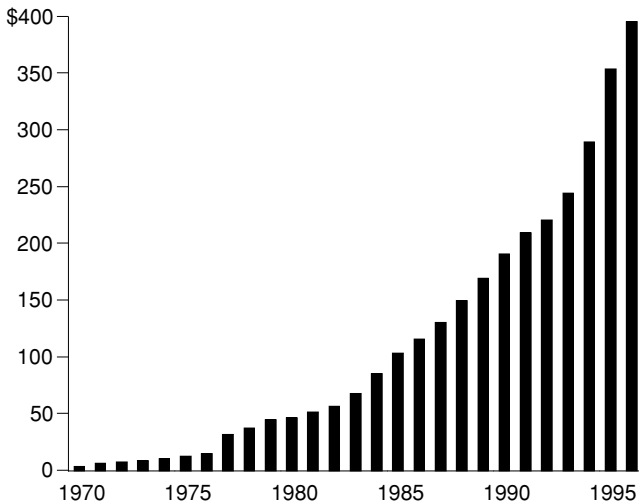
Source: Federal Reserve Board, "Flow of Funds Accounts," "Household Table," various years.

sometimes referred to as the "Anglophile East-Coast establishment" of the United States. The role of that establishment is exemplified by the British-linked Morgan banking interests in the history of Wall Street until today; by the role of other powerful Anglo-American financial families such as the

FIGURE 7

**Outstanding U.S. credit card debt, 1970-96**

(billions \$)



Sources: Federal Reserve Board, "Flow of Funds Accounts," "Household Table," various years; EIR.

Rockefellers and the Harrimans; by the "Boston Brahmin" families and the elite families of the so-called "New Confederacy" in the Southern states. These U.S. elements of the financial oligarchy were always opposed to the American System of Hamilton, the Careys, and List, and they have always been directly or indirectly allied with the British monarchy and its intelligence services. U.S. history is a history of continual struggle between the Anglophile, oligarchical tendency, and the traditional republican tendency, the latter exemplified most clearly by President Abraham Lincoln.

At the beginning of the twentieth century, the assassination of President William McKinley — a representative of the American System — and the accession to power of the Anglophile President Theodore Roosevelt, helped tip the balance in favor of growing domination of the Anglo-American oligarchy. Nevertheless, the influence of the American System remained powerful into the 1960s, and even beyond. One reason was, that the establishment considered it necessary to maintain a strong industrial base for military and other strategic reasons. This began to change, however, under the influence of the strategic doctrine promoted by the British aristocrat Bertrand Russell.

Russell argued that the unlimited progress of science and technology had created a threat to human survival, in the form of nuclear weapons in the hands of sovereign governments. As long as sovereign nations were able to freely develop their own industrial capabilities and scientific research, they would ultimately be able to produce nuclear weapons. Therefore, Russell and his followers argued, the only way to make the

world safe, would be 1) to eliminate national sovereignty, in favor of a "world government" with dictatorial powers; 2) to stop the spread of industrialization, and limit access to industrial technology; 3) to eliminate scientific and technological progress itself, or at least place it under strict control. The first essential step would be to bring the United States and Soviet Union into a process of negotiation on "worldwide arms limitation."

In reality, Russell's whole argument was a deliberate fraud, aimed at dealing a death blow to the influence of the American System, and restoring the British Empire's oligarchical system under a new guise.

The first breakthrough for Russell's policy, came with the agreements made during 1958-59 between the Russian and U.S. governments under Khrushchov and Eisenhower. Although their profound impact on Western economic policy only became fully clear in the subsequent decades, these agreements already gave an important push toward abandoning the policy of broad-based scientific and industrial development, and adopting the "post-industrial society" policy instead. This tendency was clearly stated, for example, in a book published in 1960 by James Schlesinger, who later became Secretary of Defense under President Carter. The book was titled *The Political Economy of National Defense*. Schlesinger argued that in the era of nuclear weapons, full-scale wars had become impossible; therefore, military power no longer depended on maintaining a large industrial infrastructure and workforce. He also called for the United States to stop its policy of helping developing nations to acquire advanced technologies, such as nuclear technology for peaceful purposes (President Eisenhower's "Atoms for Peace" program).

By the middle of the 1960s, it was clear, that the Anglo-American establishment was fully committed to Russell's policy and the transition to a "post-industrial society." The death of Kennedy marked a turning point in this process. From that point on, the oligarchical faction was able more or less to dictate much of U.S. economic, financial, and foreign policy, with relatively weak resistance from what remained of the American System faction. Under the shock of the present financial collapse, however, that situation may shift again, in the opposite direction.

### III. The cancer of the world financial system (1967-98)

The transition period ends in 1967, with the beginning of a series of explosive monetary crises within the Bretton Woods system, exactly as LaRouche had warned.

Undoubtedly, a major contributing factor was the inflationary effect of deficit spending for the Vietnam War, as well as the massive expansion of consumer credit in the United States from the late 1950s into the 1960s, at a time when continental European countries still continued on a course of capital-intensive industrial development. However, as subsequent developments make clear, the late 1960s crisis of the

Bretton Woods system was not a temporary or merely cyclical phenomenon. The fundamental shift away from the successful American System orientation of the immediate post-war period, planted a deadly cancer into the world economy. In the course of the following 30 years, the cancerous process produced the largest bubble of fictitious, speculative values and unpayable debt, ever known in human history.

For the purposes of analysis, it is convenient to divide the evolution of the global financial crisis from 1967 to the present, into the following periods:

**1967-71:** From the British sterling crisis of 1967; through the explosion of the dollar crisis in March 1968; the deepening recession in Europe; to the decoupling of the dollar from gold in August 1971.

**1972-79:** From the transition to “floating exchange rates” and outbreak of massive currency and commodity speculation; through the mid-1970s “oil price shock,” which launched the Third World debt crisis, and the rapid expansion of the Eurodollar market and “petrodollar recycling”; to the “interest rate shock” beginning October 1979.

**1980-87:** From the U.S. industrial collapse, brought on by high-interest-rate policy; through the Ibero-American debt crisis of 1982-83; the imposition of IMF conditionalities policy on Mexico and other Third World countries; the “Reagan recovery” based on massive pumping of liquidity into financial markets; the launching of the bubble economy in Japan; radical financial deregulation in the United States, Great Britain, and other nations, and the launching of the speculative “junk bonds” bubble; to the October 1987 market crash.

**1988-91:** From the take-off of the financial derivatives bubble, through the acceleration of radical liberalization, deregulation, and globalization policies under George Bush and Margaret Thatcher; the breakdown of the U.S. system of savings and loan institutions; the collapse of the “junk bonds market”; to the collapse of the Soviet Union and the consolidation of IMF control over the economic reform process in eastern Europe and the former Soviet Union.

**1992-summer 1994:** From the collapse of the productive sector in Russia and eastern Europe under IMF shock therapy, through the initial breakdown of the European Monetary System and the major wave of mass unemployment in Germany and other western European countries; to Lyndon LaRouche’s “Ninth Forecast,” warning of the inevitable disintegration of the global financial system.

**Fall 1994-98:** From the collapse of the Mexican financial system (beginning December 1994) and the initial outbreak of the Japanese banking crisis; through the period of uncontrolled asset-price inflation on world stock markets and other markets; to the explosion of the Asian financial crisis, which is now spreading to the rest of the world.

Within this 30-year historical process, the disease of the financial system went through a series of stages, each marked by major crises which had to be addressed by governments and leading financial institutions. The history shows, that at

each crucial turning point, the decisions that were taken made the underlying problem even worse, creating the preconditions for even more serious crises at the next stage. The common feature of these decisions, was to try to “solve” the problems created by the growing bubble of debt and speculative financial assets, by sacrificing more and more of the real, physical economy in order to “feed” the bubble, while successively removing the barriers to its further growth. It is like a man who tries to save his house from burning down, by throwing his furniture into the fire.

This irrational, self-destructive behavior of governments and leading institutions, including in the United States, constitutes the most remarkable feature of the last 30 years of economic history, requiring a profound analysis of cultural and other factors determining policymaking in the post-war period. Evidently, the reasons for the disease of the world financial system, and the fact that the disease has been tolerated for so long, are connected with deep-seated errors in the habits of thinking of governments and leading institutions in many countries.

We shall now focus our attention on some of the most important turning points in the growth of the “financial cancer” in the world economy. We shall pay special attention to the actions taken by governments at various stages, and the effects of those actions. In next week’s issue, we shall provide a chronological account of the most important financial and economic events relevant to our topic.

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## Turning points

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### **1967-71 monetary crisis and the transition to a neo-Malthusian economic policy**

I have already described how the fundamental policy-shift begun in the 1964-66 period, combined with the inflationary effects of the Vietnam War and other factors, created the conditions for a series of monetary crises, beginning with the 1967 collapse of the British pound sterling. Unfortunately, the response to the 1967-71 monetary crises, was *not* to return to policies of healthy industrial development that would have restored the value of the dollar and stabilized the Bretton Woods system. First, U.S. President Johnson in March 1968, and then again, three years later, U.S. President Nixon — under advice from then-Undersecretary of Treasury Paul Volcker, George Shultz, Milton Friedman, and others — gave the signal for “decoupling” the financial system from the real economy. This was done despite the fact, that French President de Gaulle’s economic adviser Jacques Rueff and others had put forward alternative policies, which could have saved the dollar and restored healthy development in the world economy.

On Aug. 15, 1971, Nixon took the decision to eliminate the gold-reserve backing for the dollar. This put a decisive end to the post-war period of currency stability under the



original Bretton Woods system. It opened the way for a flood of currency and commodity speculation, and for introducing the system of floating exchange rates, undermining healthy long-term planning and increasing the risks of long-term international investment and trade.

Parallel with the elimination of the original gold-reserve system and fixed currency parities, regulations and policies were put into effect in the United States, which greatly accelerated the flow of dollars into offshore markets having no restrictions on interest rates and virtually no regulatory supervision. A large part of this exodus of dollars went to British Commonwealth areas, including Britain, Canada, the British West Indies, Singapore, and Hong Kong. This was the beginning of the Eurodollar market, whose center became the City of London. Through its controlling share of the growing Eurodollar market, its "special relationship" to the United States, and its powerful influence within a vast network of institutions in the British Commonwealth, London was able to retain an extraordinary degree of power and influence around the world, in spite of the loss of most of its colonies.

By 1979, more than one-third of all U.S. dollars were circulating outside the United States. These dollars became the basis for uncontrolled credit-generation by the offshore Eurodollar banks, on the basis of the so-called "Keynesian multiplier." Under conditions where the lending potential of domestic U.S. banks was restricted by policies of the Federal Reserve, increasing amounts of Eurodollar loans began to flow through Canada and other offshore centers, into the U.S. banking system. In this and related ways, the growth of the Eurodollar credit bubble became a major source of inflation in the United States and other countries. At the same time, U.S. financial policy became more and more a prisoner of the overseas dollar markets.

During this period, the anti-industrial orientation of economic policy became more and more obvious. This is revealed, for example, by the channelling of millions of dollars from the Rockefeller and Ford Foundations and other prominent American and European foundations, into "popular movements" protesting against nuclear power plants, roads, and industrial projects. With the help of this flow of funds, the student rebellion of 1968, which began mainly as a protest against the Vietnam War, was transformed into the so-called environmentalist movement of the 1970s and 1980s. A leading role in these developments was played, once again, by British strategist Bertrand Russell.

At first glance, it seems paradoxical, that powerful foundations linked to multinational companies (especially oil companies) and banks, as well as influential elements of the old European oligarchy (such as Prince Philip of England and Prince Bernhard of Holland), would support a movement directed against industrial development. Nevertheless, this is a fact, which coincides with a growing shift of investment out of production, into parasitical, non-productive sectors, and

into a speculative bubble. Actually, the shift from an industrial economy into a parasitical "bubble economy" would not have been tolerated by the population and leading institutions of the various nations involved, unless it had been prepared by a change in cultural attitudes.

### **The oil price shock of 1973-75**

Instead of bringing the "dollar bubble," including the London-based Eurodollar market, under control, the decision was made to pump it up with an enormous injection of liquidity. This was done at the expense of the entire world economy, with the help of the "oil price shock" of the mid-1970s. As the secret May 1973 Saltsjöbaden Conference and other evidence demonstrates, the huge oil price increase, following the October 1973 Middle East War, was carefully planned in advance and orchestrated by leading circles within the Anglo-American establishment, its banks and multinational oil companies, in an entirely artificial manner. The sudden, fourfold increase in oil prices created a new bubble, a bubble of Third World debt, at the same time looting the world's industrial economy in the interest of the Anglo-American banks and oil cartels.

Rather than freezing or writing off that artificial debt, the debt bubble was massively expanded in the subsequent period, by the increase of "floating interest rates" to usurious levels, and the repeated issuance of new loans to cover payments on old loans (the so-called "rollover"). This policy, together with the IMF conditionalities imposed beginning in the early 1980s, have driven most of the developing-sector economies into virtual bankruptcy, while drastically constricting the potential market for high-technology capital-goods exports by the industrial nations.

By the second half of the 1970s, the financial cancer had already reached a life-threatening stage. Nevertheless, a workable alternative policy had been put forward by LaRouche and his collaborators, and circulated among governments and leading institutions internationally. LaRouche's International Development Bank (IDB) proposal for a new, gold-reserve monetary system oriented toward large-scale infrastructure development and technology transfer to the developing nations, was placed on the table at the United Nations General Assembly in 1976. In the same period, leading industrial circles from Germany and other European nations, as well as policymakers in Japan, attempted to pursue a policy for Third World development based on infrastructure development and advanced technology. This thrust is exemplified by programs of cooperation between Germany, France, and a number of developing nations for construction of nuclear power plants, and proposals such as the Mitsubishi Research Institute's Global Infrastructure Fund.

The resistance of France and Germany against the destructive economic policies of the U.S. Carter administration

and the “floating currency rate” policy, reached a high point with the 1978 decision to establish the European Monetary System (EMS) and European Monetary Fund (EMF). LaRouche had been intensively involved in discussions with European statesmen, bankers, and industrialists on this subject since at least 1974, when he circulated the proposal for a “golden snake” of European currencies. Later, LaRouche called for the EMS-EMF to be made into the kernel of a new, worldwide monetary and financial system based on the principles embodied in the original IDB proposal. The strategy was to gain the support of the United States and to bring in the U.S.S.R. other East bloc nations, and the developing nations, at the earliest possible time.

Unfortunately, these initiatives suffered serious setbacks, including the assassination of several prominent European industrial and political leaders who had favored industrial development in the Third World. The pro-industrial current in Europe was decisively weakened by the early 1980s.

One consequence of this has been, that the present European plan for financial union and a common European currency, embodies radical monetarist, oligarchical policies which are quite opposite to the pro-industrial tendencies of the 1976-78 period.

As a result of the temporary defeat of the IDB and related policies, the financial cancer went into a new, even more lethal phase.

### **The interest rate shock of 1979**

Inevitably, serious inflationary effects resulted from the further growth of the Wall Street bubble, the Eurodollar bubble, and the Third World debt bubble. Rather than addressing the underlying cause of the problem, the newly elected Thatcher government of Britain, and soon afterward the U.S. Federal Reserve Bank under Paul Volcker, applied the ultramonetarist policy of shock therapy, by suddenly raising interest rates to the highest levels since the U.S. Civil War. This, combined with credit controls and other measures imposed by Volcker and the Carter administration, dealt a devastating blow to the industrial and agricultural base of the U.S. economy. Within a few years, hundreds of thousands of farms and medium-sized industries were ruined and driven out of business. In many areas of industrial production, the physical output of the U.S. economy declined by between 30% and 50% within three years. Even today, U.S. industry and agriculture have not recovered from the effects of the 1979-81 shock therapy. (See **Figures 8-13.**)

The effects of high-interest-rate policy were naturally not limited to the United States and Britain. The interest rate on Eurodollar loans grew from 7% in early 1978, to up to 20% at the beginning of 1980. World trade suffered its worst collapse since 1958. Above all, the interest rate increase meant an unexpected, terrible blow to developing nations, which had financed their oil imports through Eurodollar loans having



*Paul Volcker, as chairman of the Federal Reserve, raised U.S. interest rates to the highest levels since the Civil War, wiping out industry and agriculture.*

floating interest rates, coupled with the London LIBOR (interbank lending rate). Overnight, those nations had to pay more than double the amount in debt service that they had envisaged at the time the loans were made.

The deliberate nature of this shock therapy against the industrial economies and developing nations of the world, was underlined in a series of studies published by the New York Council on Foreign Relations at the end of the 1970s. The CFR, founded after World War I as an offshoot of the London Royal Institute of International Affairs, is one of the most prominent policy organs of the Anglo-American establishment. In a series of books entitled “Project 1980s,” the CFR proposed a policy to promote “a certain degree of controlled disintegration of the world economy.” One of the main purposes of this policy was to crush the forces in favor of an industrial development in the so-called “Third World,” which I have referred to above. By delivering decisive blows to the national economies of the various nations, the path would be cleared for a later phase of “globalization,” in which national economic sovereignty would be eliminated.

The impact of the interest rate shock was made even worse by a second oil shock, which followed the overthrow of the Shah of Iran in early 1979. World oil prices rose sharply again, reaching 13 times their pre-1973 levels.

FIGURE 8  
**U.S. prime interest rate, 1940 to present**

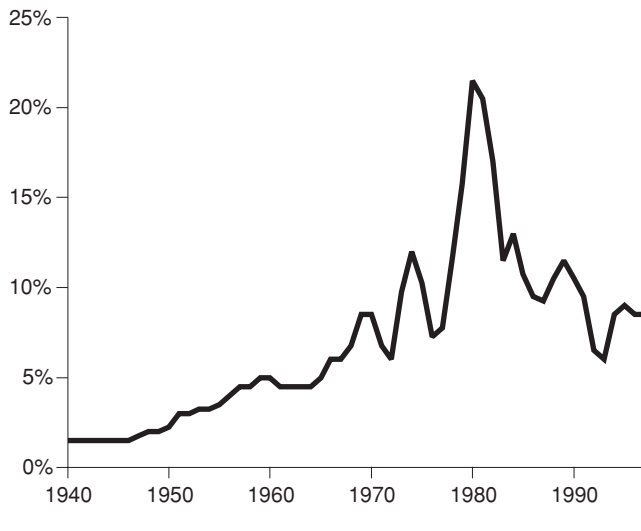


FIGURE 9  
**U.S. production of lathes, milling machines**  
 (yearly output in thousands of units)

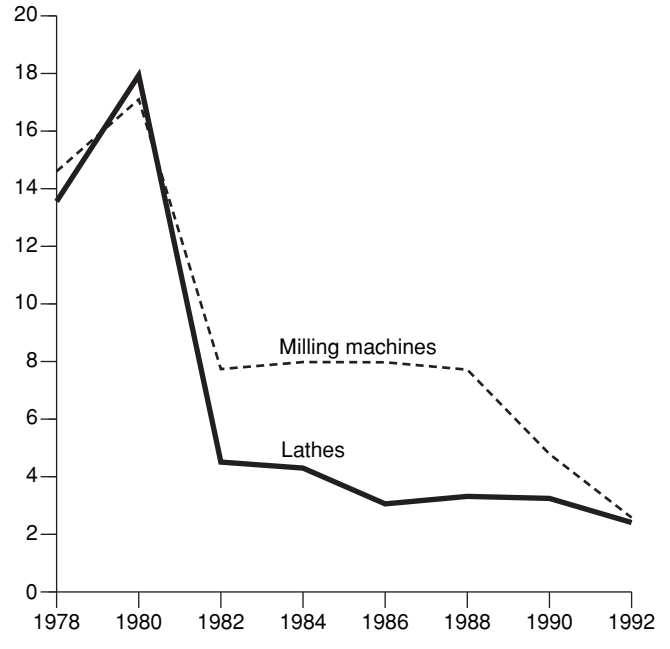
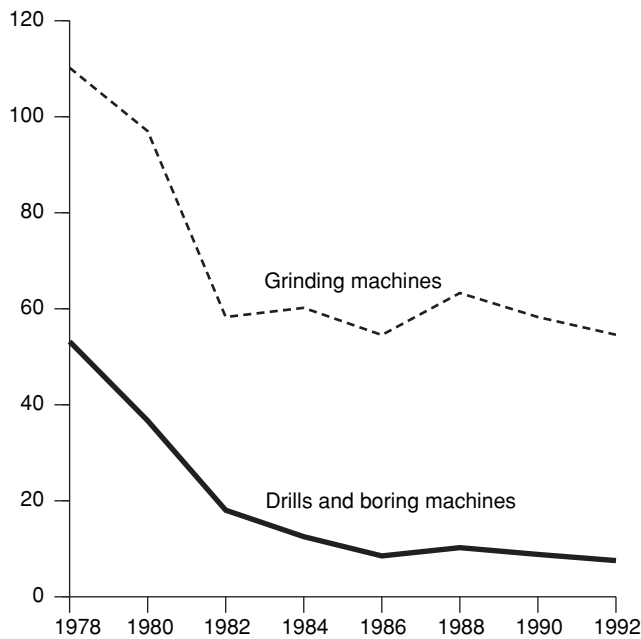


FIGURE 10  
**U.S. production of drills and boring machines, grinding machines**  
 (yearly output in thousands of units)



Source: U.N. statistical yearbook

### The Ibero-American debt crisis of 1982-83

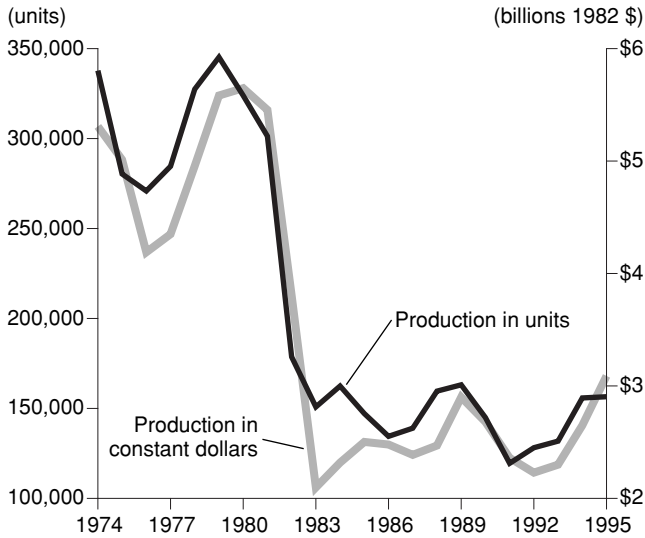
The combination of the drastic interest rate increase together with a second oil price shock in 1979, created an intolerable situation for many developing countries, and led directly to the Ibero-American debt crisis. In the four years between 1978 and 1982, the official foreign debt of the Ibero-American countries had more than doubled, from \$156.5 billion to \$322.8 billion. During the same period, more than \$78 billion in flight capital left the Ibero-American countries. All of this occurred without any significant inflow of investment to compensate for the huge losses. In 1981, the situation was aggravated by speculative attacks against Ibero-American currencies.

The strongest point of resistance to this looting process was the President of Mexico, José López Portillo. In May 1982, López Portillo met with LaRouche in Mexico City to discuss measures to save the Mexican economy. Soon thereafter, LaRouche drew up an economic plan for all of Ibero-America. This plan, entitled "Operation Juárez," centered on the proposal that the Ibero-American nations should form a "debtors' cartel" and a common market, in order to impose a fair reorganization of the debt and launch a continent-wide economic development boom based on the principles of physical economy.

By the beginning of August, when "Operation Juárez" was published, Mexico was de facto in a state of default on its foreign debt payments. Capital was leaving the country in panic, and the entire financial system was collapsing. In this

FIGURE 11

**U.S. machine tool production, in units and 1982 constant dollars**



Source: "Economic Handbook of Machine Tool Builders," various years.

emergency situation, López Portillo moved toward implementing key aspects of LaRouche's policy. To recover control over the economy, he imposed strict currency controls (Aug. 5), declared a temporary moratorium on payment of foreign debt (Aug. 22), and nationalized the banking system (Sept. 1). Parallel with these emergency steps, Mexico made urgent efforts to gain the support of other Ibero-American nations, particularly Argentina and Brazil, to join in a common policy vis-à-vis the foreign creditors. Since Mexico was not strong enough to stand up on its own economically and politically, everything depended on the response of the other countries.

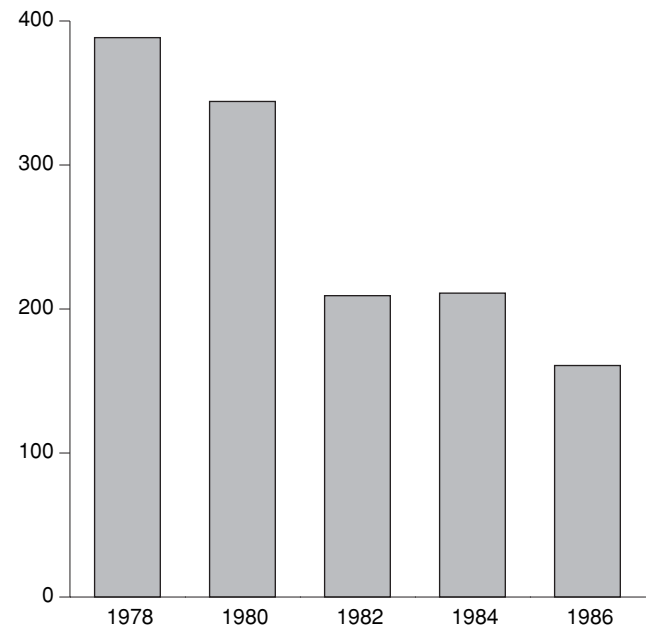
Unfortunately, due to the vacillation and cowardice of some Ibero-American governments, and massive pressure from the outside, including Britain's Malvinas War against Argentina, the historical chance to realize "Operation Juárez" was missed. One by one, the governments of the Ibero-American countries submitted to the conditions of the creditor banks and the IMF.

The policy to make the IMF into the "world policeman" for enforcing the payment of Third World debt, was already stressed on the night before López Portillo's speech to the United Nations, by U.S. Secretary of State George Shultz. Shultz proclaimed that the United States was heading for a new "economic recovery," and called for IMF management of individual nations' debt problems. This policy was expressed in the IMF's conditionalities and structural adjustment programs. Debtor countries would be forced to carry out drastic devaluations, to eliminate state subsidies for food and other basic commodities and production sectors, and to

FIGURE 12

**U.S. diesel motors production**

(yearly output in thousands of units)

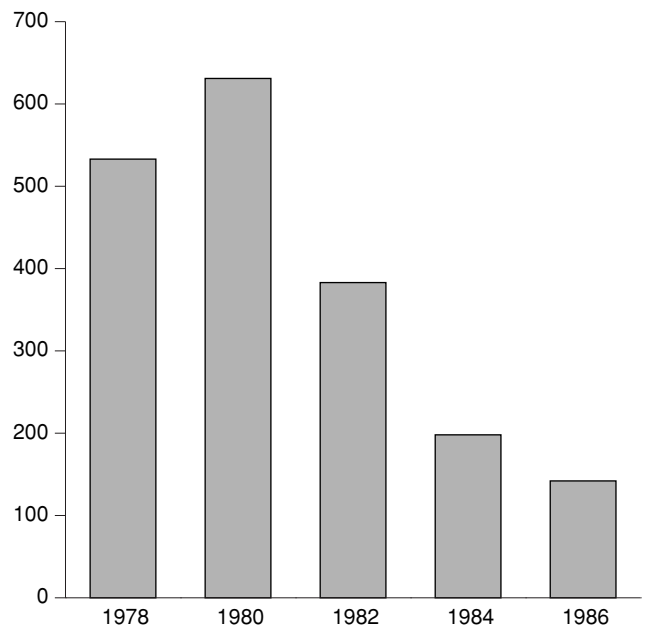


Source: U.N. statistical yearbook

FIGURE 13

**U.S. production of forging and stamping machines**

(yearly output in thousands of units)



Source: U.N. statistical yearbook



*President Reagan with Mexican President José López Portillo, June 1981. One year later, López Portillo attempted to implement LaRouche's "Operation Juárez" plan, but the failure of other Ibero-American governments (and the United States) to support him, meant that the strategic opportunity was missed.*

make severe cuts in public spending. In each case, the effect of the IMF's programs was to collapse living standards for the majority of the population, suspend net investment into the productive base of the economy, and vastly increase the burden of debt through devaluations of the national currency. (See **Figures 14-16.**)

From the standpoint of the claimed purpose of solving the debt problem, the IMF policy has been a miserable failure. On the other hand, the policy did lead to a gigantic looting of Third World nations caught in the "debt trap." By the mid-1980s, the developing countries were supplying tens of billions of dollars per year in net capital flow to the industrial countries, and especially to Anglo-American financial institutions. According to UNICEF, the net capital flow from poor nations to rich nations grew from \$6 billion per year in 1983 to \$30 billion per year at the end of the 1980s. Taking into account the dramatic drop in raw materials prices, the real, physical-economic cost to the developing countries was at least double that. In addition, the total amount of capital flight from developing nations to the industrial nations, in the course of the 1980s, is estimated at more than \$400 billion.

Despite this enormous capital flow out of the Third World countries, the debt continued to increase. According to World Bank figures, in 1980 the total external debt of 109 developing countries, including private and public debt of more than one-year maturity, was approximately \$430 billion. Payment of interest from 1980 to 1986 totalled \$320 billion, and repayment of principal \$332 billion. Thus, Third World countries paid a total of \$658 billion between 1980 and 1986, on an original debt of \$430 billion. Yet, the total debt outstanding

in 1986 was \$882 billion! Only a small part of this increase was connected with additional, real credit issuance for new investment; the growth of the debt bubble was almost entirely a result of the high interest rates and the roll-over of old debt by means of new loans. By 1994, the debt of 109 developing countries had grown to \$1.6 trillion.

In the case of Mexico, López Portillo's national-economic policies were soon reversed. Subsequently, the successive "solutions" imposed by the IMF and the creditor banks, including the "Brady Plan," had the effect of only delaying the full onset of the crisis, while making the underlying problem worse. This laid the basis for the explosion of the Mexican financial system in December 1994.

### **The 'Reagan recovery,' the 'bubble economy' in Japan, and the growth of the drug trade**

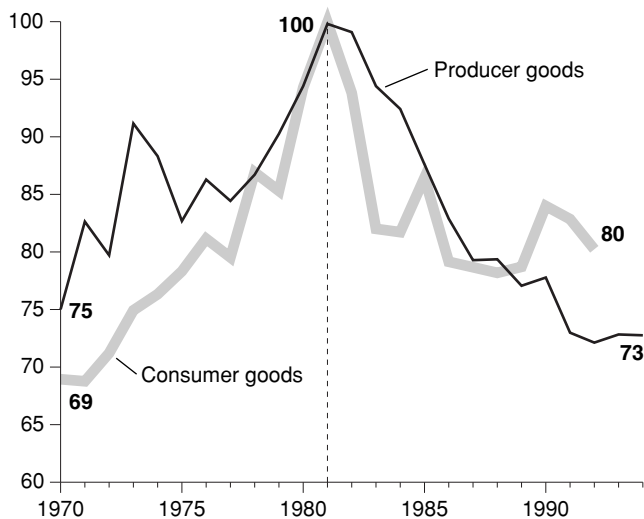
President Reagan had been elected as the result of a popular reaction against the destruction of the U.S. economy under Reagan's predecessor, Jimmy Carter. With the productive base of the U.S. economy devastated by the effects of the interest rate shock, the urgent requirements for the United States were to channel credit and investment back into industry and agriculture, to revive the nuclear and other advanced technology sectors, and to rebuild the nation's basic infrastructure. LaRouche, who had played a leading role in promoting the policy of rebuilding and modernizing the U.S. economy for many years, became intensively involved in discussions with inner circles of the Reagan administration, concerning future economic policy for the country.

In late 1981, LaRouche began to elaborate a comprehen-

FIGURE 14

**Mexico: producer and consumer goods**

(index 1981=100)

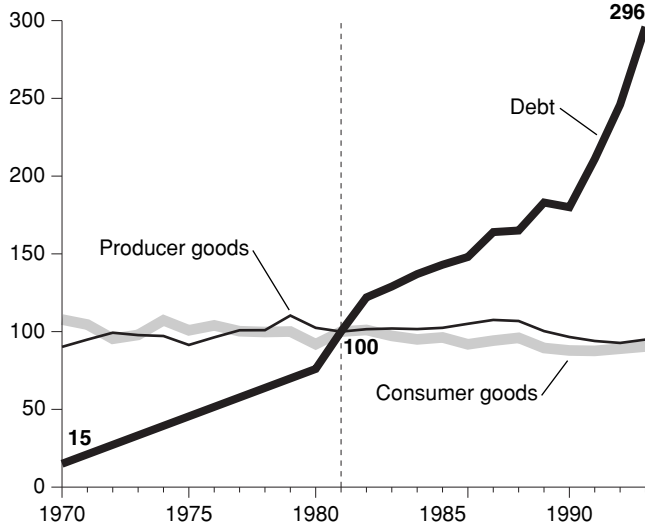


Sources: ECLAC (United Nations), INEGI (Mexico).

FIGURE 15

**Argentina: foreign debt versus consumer and producer goods production**

(index 1981=100)



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

sive policy for a technological and strategic revolution, based on development of new types of weapons systems for defense against nuclear attack. Development of these systems would involve a wide range of new technologies, including new types of lasers, high-temperature plasma and particle beam technologies, and nuclear and other advanced energy sources. LaRouche proposed using the civilian “spinoffs” of such a military program, together with a new, long-term space program aimed toward manned missions to the Moon and Mars, as a means to modernize and transform the entire U.S. economy. Key aspects of LaRouche’s policy were adopted by Reagan in March 1983, and became known as the Strategic Defense Initiative (SDI).

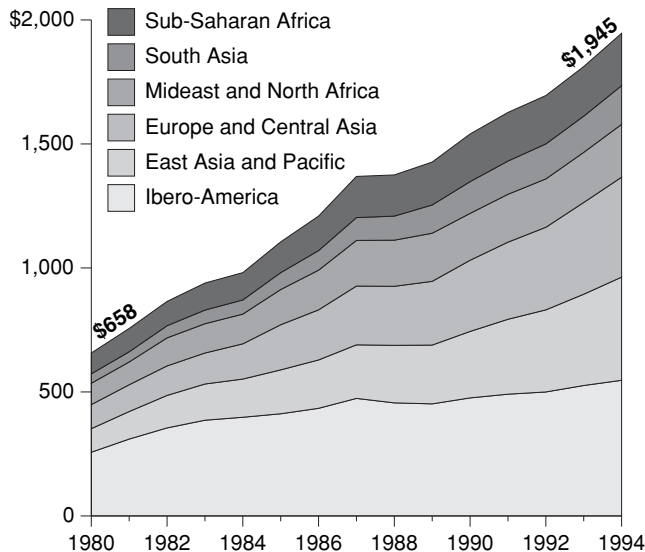
The SDI played a decisive role in bringing about the end of the Cold War, and also led to important technological developments. However LaRouche’s broader economic policy was not adopted. In fact, under the influence of the Anglo-American establishment, as typified by Treasury Secretary Donald Regan, the Reagan administration adopted exactly the opposite economic policy. Soon, LaRouche and his movement became the target of an unprecedented campaign of political persecution, which escalated into blatantly unjust legal prosecution, and finally to the jailing of LaRouche for five years, beginning 1989.

The strategy of the so-called “Reagan recovery” was to open the floodgates for an unprecedented expansion of the financial bubble. This was accomplished by 1) tripling the national debt of the United States, from \$998 billion in 1981 to \$3 trillion in 1989 (Figure 17); 2) radical deregulation of the banking and financial system, permitting high-risk specu-

FIGURE 16

**World foreign debt, by region**

(billions \$)



Source: World Bank.

lative operations on a scale which would have been unimaginable in former times (see Figures 18-20); 3) pumping up a gigantic real estate bubble in the United States, with bank loans to real estate almost doubling between 1986 and 1990; 4) permitting the takeover and savage looting of the assets of

FIGURE 17

**U.S. government debt as % of GNP**

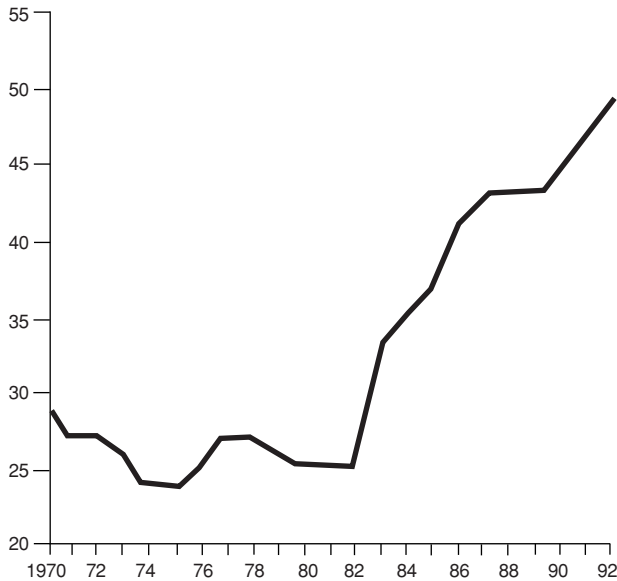


FIGURE 18

**Mergers and acquisitions versus manufacturing new plant and equipment**

(billions \$)

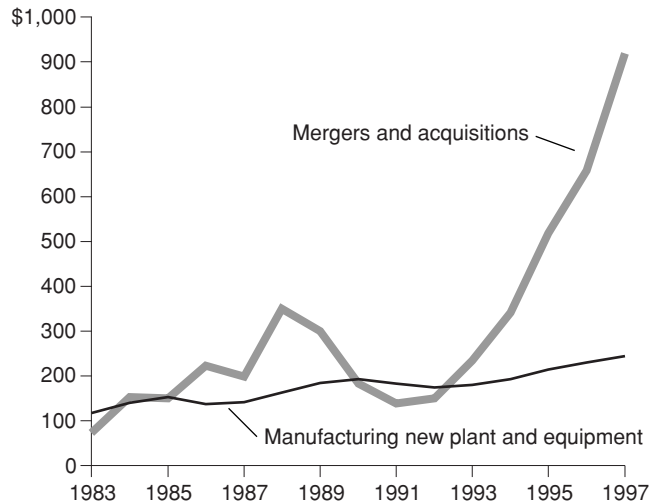
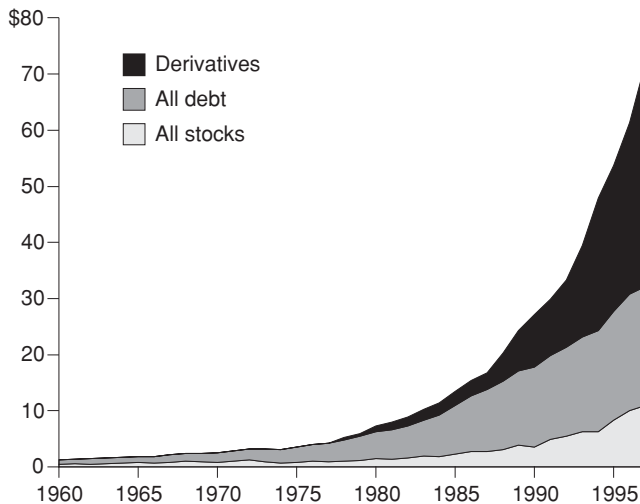


FIGURE 19

**Hyperbolic growth of the U.S. financial aggregate**

(trillions \$)



U.S. agricultural and industrial enterprises by speculators, using methods such as “junk bonds” and leveraged buyout deals (LBOs); and 5) increasing the net flow of capital into the United States, in the form of debt payments and flight capital from developing nations, as well large imports of funds from Japan and western Europe.

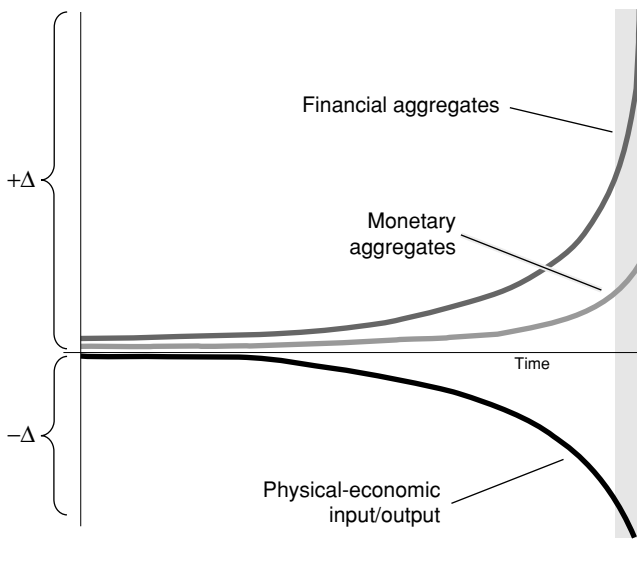
A direct product of bank deregulation in the United States was a bubble in the system of more than 3,000 savings and loans associations in the United States. The operations of the S&Ls were formerly restricted mainly to financing long-term purchases of homes at low interest rates which were fixed by law. These and other restrictions were removed by a new law in 1982. The resulting competition for investors and depositors, and other factors, pushed these banks into wild speculative practices. During the second half of the 1980s, the real estate bubble went into a collapse, and the S&L system was virtually bankrupted. By 1989, more than 400 thrift institutions were declared insolvent, while others were only saved by emergency mergers and an injection of over \$300 billion of government funds.

But, this was only part of the wild ups-and-downs of speculative activity, which reached a fever pitch in the period leading up to the stock market crash of October 1987. In the course of the 1980s, encouraged by deregulation and changes in tax laws, a new epidemic of speculation and looting broke out on Wall Street, in connection with the so-called junk bonds and leveraged buyouts. Typically, companies were taken over by speculative raiders using borrowed money, and the resulting debt was loaded onto the victim company, to be paid at the expense of selling off assets, closing down factories, and firing workers. These speculative looting operations were often connected with issuing high-risk, high-yield speculative “junk bonds,” often leading to unpredictable shocks and sudden bankruptcies.

Instead of intervening to stop this orgy of parasitical speculation, which was rapidly destroying what remained of the

FIGURE 20

**A typical collapse function**



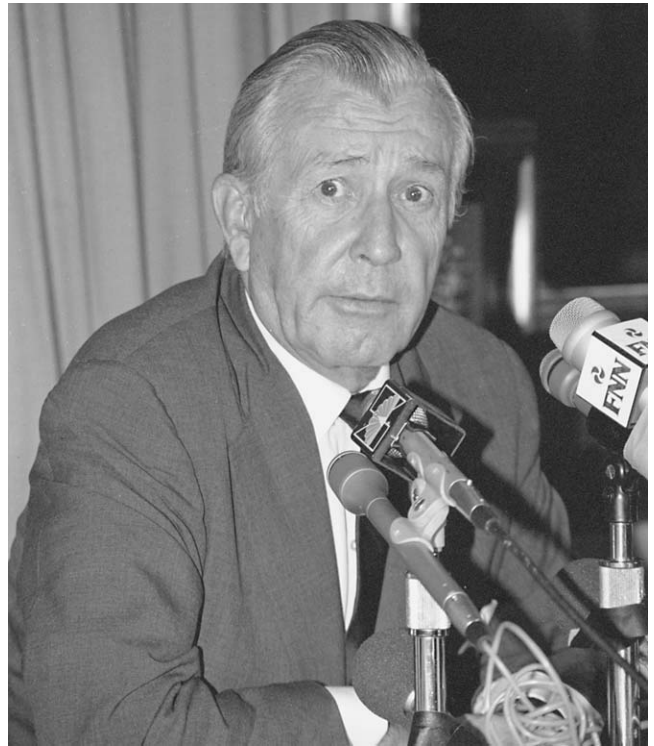
*LaRouche's "triple curve" schematic shows how the hyperbolic growth of financial and monetary aggregates ("the bubble") proceeds at the expense of the physical economy, until a point of blowout is reached.*

healthy American industrial companies, the government actively encouraged the speculators, and took steps to extend the bubble overseas. Japan was an important part of this process.

According to a commonplace myth, the spectacular growth of the annual Japanese trade surplus to the United States — which rose from less than \$20 billion in 1982, to over \$40 billion in 1985 and over \$50 billion in 1986-89 — was the result of unfair Japanese trade practices. The main cause, however, was the collapse of the U.S. industrial base which resulted from the 1979 interest rate shock and other anti-industrial policies of the Carter, Reagan, and Bush administrations. Apart from the huge import of automobiles, the U.S. economy had become dependent upon large supplies of industrial equipment from Japan and Germany.

Enormous pressure was exerted on Japan, to help prop up the U.S. "recovery" by channelling hundreds of billions of dollars into the U.S. financial markets and by pumping up a new financial bubble in Japan. This process was greatly accelerated following the Plaza Accords of September 1985. External pressure aggravated the effect of a fundamental cultural shift inside Japan itself, as shallow-minded young professionals moved in to replace the older elite that had rebuilt Japan after the war.

At the same time, the Japanese banking system, which had traditionally been oriented to physical trade and industry, was sucked more and more into the spectacular real estate bubble in Japan and some other parts of Asia. The total loans



*U.S. Treasury Secretary Donald Regan's policies toward Japan, including the September 1985 Plaza Accords, helped pump up a financial bubble there, which is now blowing out.*

of Japanese banks quadrupled between 1985 and 1990, while the percentage of loans going to the productive sector shrank from 38% to only 25%. (In 1965, fully 63% of all lending of Japan's top 150 banks went into the productive sector.) This set the stage for the Japanese banking crisis of the 1990s. (See **Figures 21-25.**)

In 1994, Japanese economist Mitsuhiro Seki described the 1980s process of structural decay of the Japanese economy in the following words: "For the Japanese economy the recession began with the Plaza Agreement of 1985. An abnormal spiral of land prices resulted. . . . Instead of major factories, apartments, skyscrapers, parking, houses, and office buildings were built up, leading to a disintegration of the industrial structure. . . . Since 1991, the big concentrations of small factories, which had been responsible for basic technologies, began to disappear."

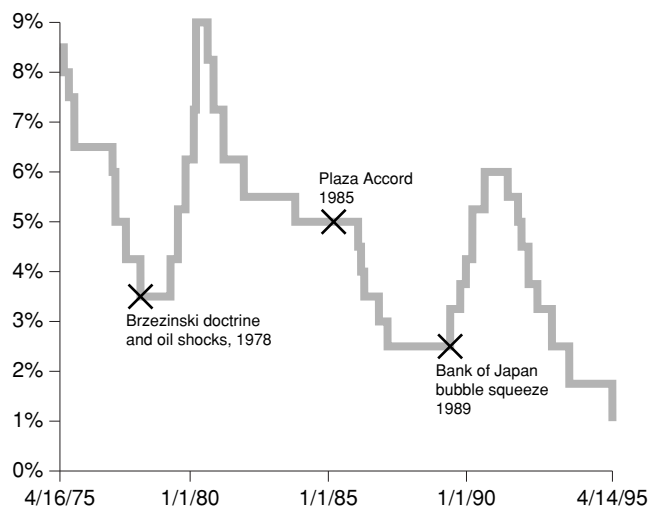
After Britain, Japan became the second largest foreign source of financial support and capital for the United States. In 1988, for example, Japanese investors covered 40% of the new issuance of U.S. debt. Japanese financial institutions also became a major source of capital for the five-year epidemic of junk bonds and LBOs on Wall Street.

The shift of policy which had led to the bubble economy in Japan, naturally had negative effects in Southeast Asian and other countries. In the course of the 1980s, the orientation toward long-term industrial and infrastructure investment



FIGURE 21

### Bank of Japan central bank discount rate, 1975-95

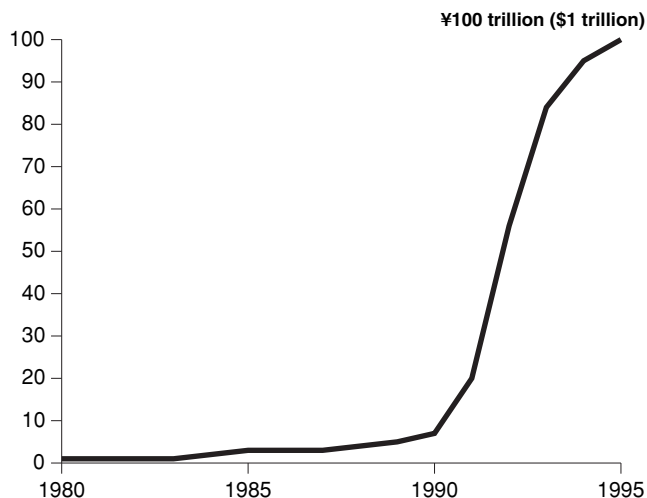


Source: Japan Ministry of Finance.

FIGURE 22

### Bad Japanese bank loans

(trillions of yen)



Sources: EIR estimates; Merrill Lynch, Tokyo; Salomon Brothers Tokyo; Standard & Chartered Bank, London.

was weakened, in favor of a policy of bringing in “quick money” by establishing offshore financial centers and “emerging markets.” This began relatively early in Thailand, which already came under strong IMF control in 1980. Indonesia and Malaysia, which had benefitted from a large income from oil exports, were hit hard by the collapse of oil prices in 1986. By the beginning of the 1990s, the “new tigers” of Southeast Asia were being fully integrated into the global bubble of “emerging markets.” Although these economies had significant problems to begin with, it was financial globalization that undermined government control and provided the leverage for speculators to destabilize and destroy national financial systems.

Another very significant phenomenon of this period is the spectacular growth in the illegal drug trade. According to rough estimates published by *EIR*, the total sales value of the illegal drug trade grew from about \$175 billion in 1977, to \$558 billion in 1989. This is a very significant figure compared with total world trade, and demonstrates why funds from the illegal drug trade necessarily play an important role in the overall capital flows within the world financial system. In fact, it can be demonstrated that the deep involvement of certain prominent banks and financial families in the management of the multibillion-dollar world illegal drug trade, has continued in an unbroken line, since the time of the British Opium Wars.

There is no doubt, that the failure of governments to take effective action against the expansion of the illegal drug trade during the 1980s, is closely connected with the policy of maintaining and supporting the speculative bubble. It was even

stated openly by some U.S. financial experts in press interviews in the 1980s, that strong measures against laundering drug funds by major banks, would threaten the stability of the banking system!

In the case of the Ibero-American countries, an intimate relationship developed between the 1) the debt crisis; 2) the growth of illegal drug production and the power of the local drug lords; and 3) the growth of terrorism and organized insurgency. It is an ugly fact, that the growth of illegal drug consumption in the United States, particularly the epidemic of cocaine use in the 1980s and 1990s, provided a huge and growing market for drug exports from Colombia, Peru, and other Ibero-American countries; and the receipts from drug exports by those countries indirectly provided a major source of funds for paying the debt. The cocaine production of Peru, Colombia, and Bolivia grew by 30-50% from 1980 to 1988.

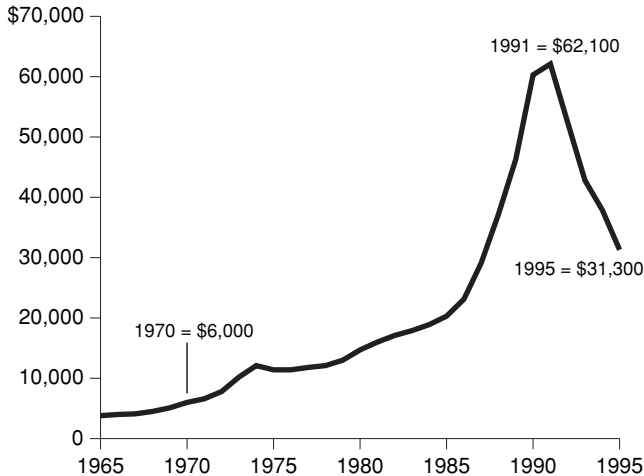
At the same time, the IMF’s “structural adjustment” policies and other policies imposed by the creditor banks, greatly weakened the national governments, collapsed living standards of the majority of the population, and in that way contributed to the power of the drug-mafia and terrorist insurgency movements. In fact, as the term “narco-terrorism” suggests, there is a very strong connection between the drug mafia and certain insurgency movements in the Ibero-American countries. Together, these processes acted to weaken and destroy the resistance of national institutions against the continued looting of their countries under IMF control.

Some economists, who helped to design and carry out the IMF policies in Ibero-America, were well aware of these facts. One example is Harvard economist Jeffrey Sachs, who

FIGURE 23

**Japan's urban real estate price bubble**

(urban real estate prices, \$ per m<sup>2</sup>)



Sources: Japan Ministry of Finance, Bank of Japan, *Japan Statistical Yearbook*.

later became a leading promoter of shock therapy in the former Soviet Union. One of Sachs's early successes was his work as an economic adviser to the Bolivian government, where he practiced a form of shock therapy as a cure for inflation. Sachs's policies were indeed successful in reducing inflation, but they led to a severe collapse of production and employment—except in the sector of illegal drugs. Sachs himself wrote that his recommendation to close down numerous state-owned mines, helped to build up the drug economy: Left with no other source of income, many of the unemployed mine workers had no alternative, but to go to work in coca production. This true story illustrates a general characteristic of the global financial cancer: The growth of the cancer is fed by a process of self-destruction or auto-cannibalization of the moral and physical substance of society.

**The crash of October 1987, globalization, and shock therapy in Russia**

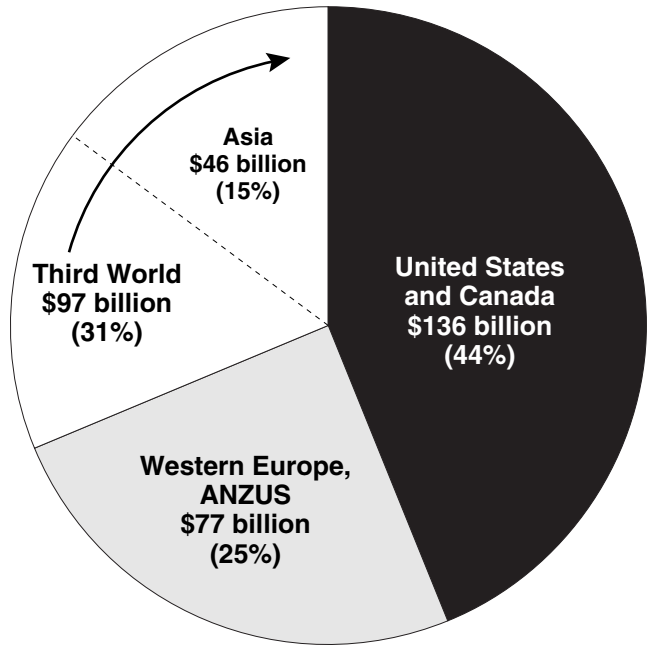
On Black Monday, Oct. 19, 1987, the Dow Jones Industrial Average collapsed by 508 points, the largest fall in history. This event should have been a signal, to reverse the policies which had led to the speculative bubble, to return to the pre-1966 emphasis on physical economy, and to carry out a global financial and monetary reform.

Unfortunately, no significant such actions were taken, and the financial cancer went into a new stage. On the one side, a new form of speculation, "financial derivatives," began to take a dominant position in world financial transactions. On the other side, the search for additional flows of income to feed the bubble became more and more desperate.

FIGURE 24

**Where Japan put its money: foreign direct investment (FDI), 1951-90**

(billions \$)



**Cumulative global total = \$311 billion**

Sources: Japan Ministry of Finance, Bank of Japan, Export-Import Bank of Japan, Japan Overseas Economic Cooperation Fund.

Indeed, the fever pitch of looting of industrial assets in the United States and other countries through junk bonds and leveraged buy-outs, reflected the fact that the existing flows of monetary profits were no longer sufficient to sustain the speculative bubble. One sign of this was the collapse of the junk bond bubble in 1989, following the bankruptcy of the giant Campeau company. In spite of repeated attempts by the U.S. Federal Reserve to increase liquidity by lowering interest rates, the collapse process in the United States continued unabated. By 1990, some of the most famous American companies had gone bankrupt, including the Wall Street investment company Drexel Burnham Lambert; the airlines TWA, Pan Am, and Continental; and banks such as the New England Bank. Another aspect was the trend toward collapse of real estate prices in the United States and other countries, leading to a series of crises in the banking system as a whole.

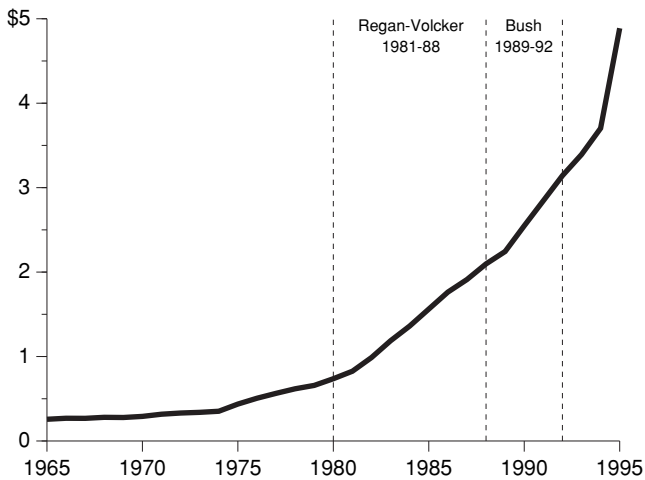
The pressure to open up new sources of income to feed the bubble, became more and more the determining factor in international policy.

1. Japan was pushed to pump more money into the U.S. financial markets. Following the October crash of 1987, the Japanese Central Bank continually lowered interest rates, encouraging money to flow into U.S. Treasury bonds and other

FIGURE 25

## Don Regan and Paul Volcker create the U.S. national debt

(total U.S. national debt, trillions \$ at end of year)



Sources: IMF, U.S. Treasury.

U.S. investments. This contributed significantly to holding the dollar stable through the U.S. election year 1988.

2. Another reaction to growing pressure from the bubble, was to force through globalization of the world economy as fast as possible, including radical liberalization of currency, capital, and commodity markets, thereby removing all remaining barriers to the metastatic spread of the financial cancer. This was the reason for the rush to conclude the Uruguay Round of negotiations under the General Agreement on Tariffs and Trade (GATT), and especially to force through a radical liberalization of world agriculture, thereby opening up the prospect of enormous additional income flows through the multinational companies that dominate world food trade.

3. An additional element was the policy of radical privatization of state-owned industries and infrastructure: This policy had been applied in Great Britain already at the beginning of the 1980s, by Prime Minister Thatcher. But the big breakthrough in privatization internationally came in Ibero-America ten years later: Revenues from the sale of state assets there soared from \$1.4 billion in 1989, to \$7.3 billion in 1990, to \$18 billion in 1991. Most of this came from Mexico; later, increasing amounts came from Argentina, Brazil, and others. Although the income from liquidation of state assets was small compared to the foreign debt of Mexico and the other countries, it helped to stabilize the debt bubble at a point where the real physical economy of the Ibero-American countries was sinking into depression.

A much larger potential source of income for the global financial bubble, however, was provided by the collapse of the Soviet Union and the opening up of the eastern European

markets. The decision as to what kind of economic policy would be applied in those countries, became a crucial issue of statecraft.

Speaking at a news conference in Berlin on Oct. 12, 1988, LaRouche forecast the collapse of the Soviet Union and the imminent reunification of Germany. He emphasized the decisive role that a reunified Germany should play in the economic reconstruction of eastern Europe. Over the following year, LaRouche and his collaborators drew up a comprehensive policy to launch an “economic miracle” in eastern Europe, based on large-scale investments in high-technology transport, energy, water, and communications infrastructure. According to this “Productive Triangle” program, East and West Europe would be integrated by a network of infrastructure corridors, centered on new, high-speed rail links. The key to realizing this policy, LaRouche emphasized, would be a reform of European banking and finance policy, along the lines he had originally proposed for the European Monetary System in 1978-79.

LaRouche warned: “Up to now, Europe and Japan have managed to shield themselves from the insanity, which has governed the financial policy of the U.S.A. and Great Britain for the past 25 years. But now the point is being reached, at which the collapse of the Anglo-American and international financial system, together with the crisis of the Soviet system, will produce an unavoidable depressive effect on Europe, Japan, and other regions. If the Europeans and Japan continue to hold onto the present form of banking and finance, then there will no longer be any island of stability. The general collapse into a global depression will be worse than anything this planet has experienced during the present century.”

In the crucial years 1989-91, there was considerable potential support for the “Productive Triangle” in both East and West Europe. LaRouche’s warning was echoed, in part, by Alfred Herrhausen, head of Germany’s largest bank, Deutsche Bank. Herrhausen was sharply critical of IMF policies and the idea of shock therapy for eastern Europe. Instead, he recommended that Germany’s state bank, the Kreditanstalt für Wiederaufbau, which played a crucial role in the reconstruction of West Germany after World War II, should be used as a model for the establishment of development banks for eastern Europe. Later, in a different way, part of the “Triangle” policy was adopted by the president of the European Commission, Jacques Delors, in his infrastructure plan for Europe.

However, there was also fierce resistance to this policy, especially from Great Britain. As LaRouche emphasized, a new, industrial development boom in Eurasia would mean a complete break with prevailing Anglo-American policies; it would not only interfere with the flow of capital into the financial bubble; just as important, the resulting economic alliance among Germany, Russia, and eastern Europe was seen as absolutely unacceptable to British strategic interests. This was repeatedly stated by Prime Minister Thatcher and other British spokesmen in 1989-90. The British applied all possible

means, including their strong influence with the Bush administration, to sabotage the “Triangle” policy and to impose globalization on eastern Europe and the former Soviet Union.

The main instrument to accomplish this was the IMF and its shock therapy policy, which was implemented in one form or another in Russia and practically all the nations of eastern Europe, starting with the famous “Polish model.”

For the former Soviet Union, especially, the shock therapy policy was practically equivalent to economic suicide. Starting in 1991, it led within a few years to 1) an explosion of hyperinflation, which eliminated virtually the entire savings of the population within a short time, and the subsequent, rapid “dollarization” of the economy; 2) flooding the domestic market with foreign goods, ruining domestic producers; 3) dependence on imports for over 60% of the food supply; 4) transfer of a large part of the nation’s assets into the hands of a small number of super-rich Russians and foreign interests, with a strong role played by organized crime; 5) drastic reduction of the level of education, scientific research, and health services, and the explosion of crime and of mortality due to diseases; 6) collapse of physical production and of investment to 30-40% of pre-reform levels, or less, depending on the production sector; 7) destruction of a large part of the technologically most advanced industries; 8) large-scale liquidation of stockpiles of physical assets (particularly raw materials and processed materials), and their sale on the world market at prices far below their real cost of production; and 9) a huge growth in Russia’s foreign debt.

The disastrous failure of the economic reforms in Russia and eastern Europe, from the standpoint of production and living standards, cannot be explained only on the basis of internal problems left over from the old system in those countries. Unfortunately, from the very beginning, the economic reform in these countries was dictated by the policy of the Thatcher and Bush governments and Anglo-American banking institutions, to feed the financial bubble at all costs. It is difficult to find reliable estimates, but there is no doubt, that the net transfer of wealth from the former Soviet Union to the West, amounts to over \$200 billion over the last seven years.

### **The German economic crisis, derivatives, and the metastasis of the financial cancer**

As LaRouche had warned, the failure to realize the “Productive Triangle” policy ensured that the western European economies would plunge into a major economic crisis. In fact, Germany and France are now suffering from the worst economic crisis since the 1930s.

Relatively speaking, in 1989 West Germany was still a modern, efficient industrial economy — especially compared with the United States and Britain. Six years later, the situation changed dramatically. Between 1991 and 1995, industrial employment in the western part of Germany decreased by 20%. In the machine-tool sector, which was the traditional foundation of West Germany’s industrial strength, employ-

ment declined by 40%. During the same period, industrial employment in eastern Germany dropped by two-thirds; by early 1997, eastern Germany accounted for less than 5% of the industrial output of the whole country. Today, the official unemployment rate is 21% in the eastern part of Germany, and 10% in the western part (the real unemployment is much higher). This is the worst in the entire post-war history of Germany, higher than in the worst period of the 1930s Depression. Meanwhile, the financial situation of the German federal, state, and local governments has deteriorated rapidly. In the attempt to reduce expenditures, the state has greatly aggravated the crisis in the construction sector and other sectors which depend on public investment, thereby increasing unemployment and reducing the tax income even more.

The situation in France and most other European countries is equally serious, and in some respects worse, because of the lower average living standard. The unhealthy state of the French financial system became very clear with the de facto bankruptcy of the largest European bank, *Crédit Lyonnais*, at the beginning of the 1990s (it has been kept from official bankruptcy only by a long series of rescue packages from the French government).

Some people, some experts, have voiced the opinion, that the crisis in Germany is a result of the reunification of the East and West, particularly the high costs of rebuilding the economy of the eastern part. This explanation is not accurate. Under different international circumstances, the reunification would have led to a huge economic boom. The main causes of the crisis have been the following: 1) Most important, Britain decided to use all possible means to weaken Germany and to prevent a process of reconstruction and modernization of Europe in which Germany would have played the central role. 2) Under heavy pressure from the Anglo-American and French side, West Germany agreed to abandon its traditional methods of long-term industrial and infrastructure development, and instead to embrace radical free-trade policies and shock therapy for eastern Germany, eastern Europe, and the former Soviet Union. 3) Investment in eastern Europe and the former Soviet Union collapsed as a result of shock therapy, leading to a permanent drop in orders for German machinery. 4) Traditional markets for East German industry in eastern Europe and the Soviet Union were lost, as a result of the breakup of long-term trading agreements. 5) Germany agreed to abandon its tradition of industry-oriented banking, and to orient instead to the British model. This process was hastened by the assassination in November 1989 of Deutsche Bank’s Alfred Herrhausen, who had resisted pressures to involve Germany’s banking system in the global financial bubble.

With the rapid decline of Germany, together with the growing decay of Japan’s industrial structure under the influence of the bubble economy, the last two relatively healthy industrial economies in the world fell ill.

Meanwhile, thanks to the victories of globalization and the opening up of eastern Europe and the former Soviet Union,



*Deutsche Bank's Alfred Herrhausen. His assassination in November 1989 led to the demolition of Germany's traditional industry-oriented banking, and its replacement with British monetarism.*

the financial cancer entered a new phase of super-rapid, metastatic growth.

This new stage is characterized by: 1) the rapid growth of “metastases,” in the form of bubbles in the “emerging markets” throughout eastern Europe, the former Soviet Union, Ibero-America, and Southeast Asia; 2) as a result of radical globalization, liberalization, and privatization, a drastic weakening of the ability of most national governments to manage economic and financial processes inside their own countries; 3) the sharp increase in the pirate-like activity of hedge funds and other speculative financier interests, typified by those of George Soros, which have become powerful enough to challenge the governments of entire nations; 4) the growth of a qualitatively new type of speculation in the form of the financial derivatives market, whose size is now larger than the combined Gross Domestic Products (GDPs) of all the world's nations.

The increasingly open, aggressive behavior of the super-speculator George Soros, is one of the typical symptoms of the new phase of the global financial cancer.

Although Soros is often described as a “big American speculator,” he was born in Hungary and received his most important training at the London School of Economics, under the influence of Sir Karl Popper and the radical free-trade philosophy of Friedrich von Hayek. Recently, Soros even proposed reviving the British Empire, as a means to “restore

order” in the world. This is not surprising, given Soros's spiritual affinity to London, and his close association with the British bank N.M. Rothschild (which is also a key center of British intelligence), and the fact that his financial base of operations is the Anglo-Dutch offshore banking centers. Soros has also been a major financier of initiatives to legalize the sale of marijuana and other harmful drugs.

From the very beginning, Soros was one of the key figures setting up the apparatus which carried out shock therapy in the former Soviet Union and eastern Europe. Soros was a major sponsor of the groups of young, radical reformers in practically all those countries, arranging international connections and high-level support for them. He was already connected to Mikhail and Raisa Gorbachov in the late 1980s, and took the lead in promoting the “500 Days Program” of Stanislav Shatalin. Soros played a central role in organizing the international teams which directed the disastrous shock therapy in Russia and other countries.

Soros's activity in connection with shock therapy in Russia and eastern Europe, fits very well with his violent speculative attacks on the currencies of developing nations and even European currencies, and recently also the Hong Kong dollar. Soros is also quite open about using currency manipulation as a political weapon. So, for example, Soros has recently threatened to launch new attacks on the Indonesian currency, unless the government is changed to please him and his friends. He has also threatened China repeatedly.

It is obvious that Soros is not an independent figure. His “miraculous” financial strength—the fact that he is able to mobilize tens of billions of dollars behind his speculative attacks—and his ability to challenge and manipulate governments with impunity, reflect the fact that he is a high-level instrument of the financial oligarchy, and especially of the British side.

It is important to stress, that Soros is not himself the cause or source of the financial cancer. He is more like a virus which attacks a patient, after the patient's immune system has been weakened. In the case of the hedge funds involved in large-scale international currency speculation, the most important questions to ask, are: Who created the conditions under which these kinds of activities are allowed to destroy the economies of entire nations? Is there a relationship between the policy of radical liberalization and globalization of financial, currency, and commodity markets, and a policy to eliminate the independence and sovereignty of nations?

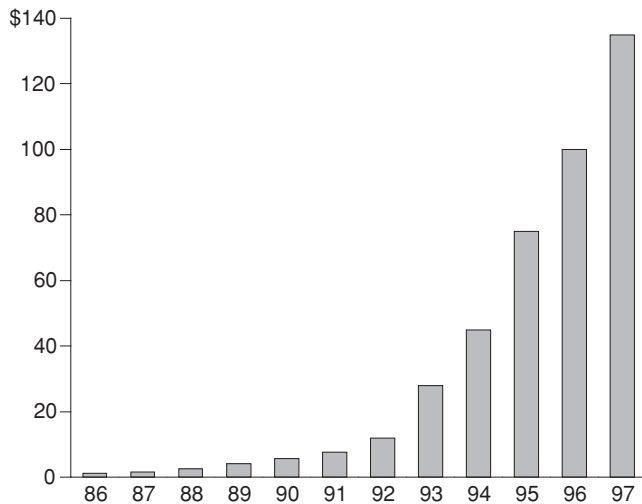
The growing frenzy of Soros, the various hedge funds, and other speculative groups is not merely due to love of power and money, and political motives. Behind it is a much bigger, much more dangerous process going on: the increasing instability of the financial derivatives market—the biggest speculative bubble in human history.

Derivatives contracts became widespread, initially, as a method of insuring against losses connected with fluctuations in currencies and interest rates. During the 1980s, and espe-

FIGURE 26

**World derivatives growth: The cancer takes over**

(trillions \$)



cially in the second half of the 1980s, derivatives contracts became prime speculative instruments themselves, completely unregulated and carried out mostly “off-balance-sheet.” As opposed to commonplace futures contracts, derivatives do not involve physical goods; they are purely financial contracts in which the two sides make an agreement to carry out a certain financial transaction at a certain future date. Depending on the nature of the derivative, the outcome of the transaction can depend on the value of the exchange rate on a specified date, or of a stock price index, or, in principle, any other parameter. A large part of derivatives contracts are connected with foreign exchange.

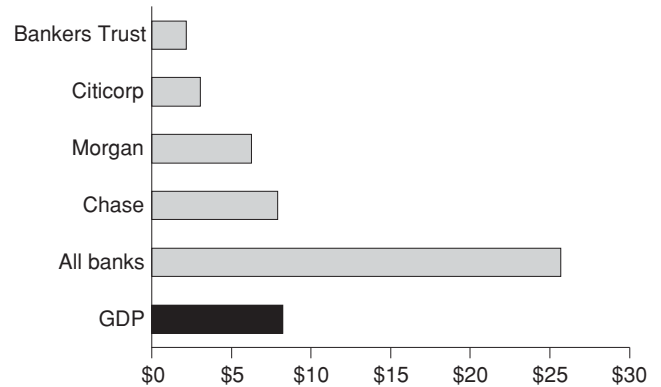
A derivative contract is basically a sophisticated form of gambling. Typically, a “player” will make a large number of derivatives contracts, in the effort to balance out the risks of speculative operations. For this purpose, complex computer programs were developed, permitting the number, scale, and complexity of derivatives contracts to develop in a way that would have been impossible in previous times.

Since 1987, the derivatives market has approximately doubled every two years. The unregulated derivatives market reached a scale which has no precedent in financial history. According to a survey of 67 banks and 12 securities firms in 11 countries, carried out by the Basel Bank for International Settlements, the total value of derivatives contracts held by those institutions at the end of 1995 was \$63.6 trillion. This is several times the combined GDPs of all the world’s nations! (See **Figures 26-27.**) derivatives bubble.] By early 1997, nominal value of derivatives contracts held by United States commercial banks alone, was \$25.7 trillion — more than three

FIGURE 27

**U.S. bank derivatives compared to GDP**

(trillions \$)



times the U.S. GDP! Many leading banks in the United States, Europe, and Japan have total derivatives contracts of the order of 5-10 times their total assets, and 100-500 times their equity.

Does this mean that the entire world financial system is already de facto bankrupt? Those who defend the use of derivatives often like to argue that the market is essentially a “zero-sum game,” where the total losses and gains among all the “players” balance out on a global level. This purely abstract argument — often used to defend speculation generally — ignores two very essential facts: 1) The gigantic size and rapid growth of the derivatives bubble is based on extremely high ratios of financial leveraging, where a given set of nominal assets becomes the basis of contracts involving many times larger sums of nominal assets; 2) the abstract “zero-sum” does not exist for the individual banks and other institutions participating in the market; as the bankruptcy of Barings Bank and many other cases show, these “players” can easily be driven into default by sudden losses many times larger than their total assets. As a result, even a relatively small disruption or dislocation within the whole, delicately balanced system of derivatives contracts, can trigger a chain reaction of defaults, which would rapidly reach such a huge dimension, that no nation or combination of nations could possibly bring the process under control. The entire world financial system would be destroyed within a very short time. This is why LaRouche has often compared the coming collapse of the derivatives bubble with the detonation of a hydrogen bomb.

**LaRouche’s Ninth Forecast**

By the middle of 1994, the global financial cancer had clearly grown to the point, where the present financial system was absolutely doomed. Nothing in the world could possibly

save it. The collapse of the physical economy of eastern Europe and the former Soviet Union, the rapid decay of Germany and Japan, and the continuing physical decline of nearly every other economy in the world—with the exception of China and a few other areas—all of this meant, that the possibility of squeezing out significant additional flows of income to support the financial bubble, was coming to an end. At the same time, the bubble itself had gone into a phase of hyperbolic growth, shooting upward toward infinity.

Looking at this reality, we can see how ridiculous it is, to imagine that a global financial collapse could be prevented by improved surveillance, improved regulations, “early warning,” or other “safety systems.”

In reality, only two possibilities remain. Either:

1. Some combination of nations, including a leading role of the United States, for obvious reasons, takes the initiative to reorganize the world financial system, by declaring it bankrupt, and establishing a new system in its place; or

2. An uncontrolled collapse of the existing system will occur, causing a complete destruction of the world economy, as well as virtually every national economy, and a descent into global chaos and war, worse than anything which has occurred in recent centuries.

This, essentially, is the alternative which Lyndon LaRouche put forward in his “Ninth Forecast,” published in *EIR* on June 24, 1994 (“The Coming Disintegration of Financial Markets”).

Since LaRouche’s Ninth Forecast, the world financial system has been hit by a series of “earthquakes” of increasing intensity. So far, the world’s governments have failed to take effective action. The consequences can be seen in the following, brief review of some important events from the time of the Ninth Forecast in June 1994, until the beginning of 1998.

On Dec. 6, 1994, the richest county in the United States, Orange County, California, went officially bankrupt as a result of a loss of approximately \$3 billion in financial derivatives speculation.

At the end of that year, the Mexican crisis broke out. The Mexican currency and financial system collapse, and a default on debt payments, were prevented only at the last moment, by an unprecedented rescue package of \$50 billion from the United States and the IMF.

Two months later, at the end of February 1995, the British bank Barings went bankrupt, as a result of losses in derivatives.

In May 1995, an “earthquake” occurred in the Japanese financial system. By the summer 1995 a secret agreement was reached between the U.S. Federal Reserve and the Japanese government, providing for \$500 billion of emergency assistance to the Japanese banking system, in case the collapse of Japanese banks would threaten to trigger a chain reaction in the international financial system. The \$500 billion guarantee was especially designed to reduce the danger that Japanese banks might begin to liquidate their holdings in U.S. Treasury

bonds, causing a financial panic inside the United States and possibly triggering a collapse of the entire world financial system. The existence of the U.S.-Japan emergency agreement was only reported much later in the press. A sudden, explosive crisis in the Japanese banking system was prevented, but the financial situation there continued to worsen, step-by-step. The total amount of bad loans in the Japanese banking system was estimated at \$1,000-1,200 billion.

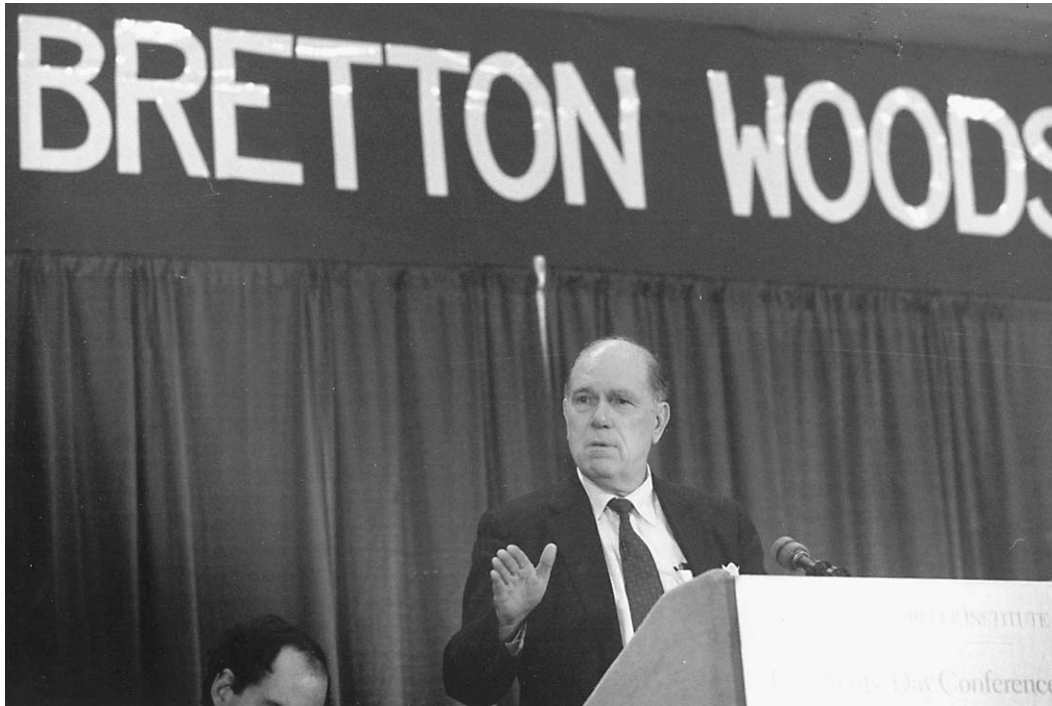
In June 1995, the danger of a systemic crisis of the world financial system was discussed at the economic summit meeting of the Group of Seven in Halifax, Canada. Instead of initiating a reorganization of the financial system, the decision was made to reflate: to inject large amounts of new liquidity into the markets, by lowering interest rates to extraordinarily low levels. In fact, from the summer of 1995 on, central bank interest rates reached historic lows. In Japan, the interest rate was lowered to 0.5%, and kept there throughout 1996 and 1997. In spite of this, the situation of the Japanese banks continued to deteriorate.

Meanwhile, however, the reflation policy led over the following two years to a spectacular growth of the values of stocks on most of the world’s markets. In the United States and some other countries, the stock market expansion created euphoria, encouraging millions of families to invest their savings into stocks and mutual funds, and even to take out large bank loans in order to invest into the stock market. At the same time, however, many indications showed that some well-informed investors, particularly connected with the British and continental European oligarchy, were quietly and gradually pulling their money out of stocks and financial paper. Instead, they were investing in “hard” commodities, such as precious metals and raw materials—anticipating a future collapse of the markets.

During this same period, euphoria was spread around the world concerning the “emerging markets,” and particularly the “Asian Tigers.” In late 1996, LaRouche warned against this euphoria, and pointed to the danger of a financial collapse in Southeast Asia. He directed his collaborators to assemble documentation of the real situation in those countries. Their report, which was published in *EIR* on Feb. 7, 1997, concluded that the physical economy of the “Asian Tigers” was weak, and their financial markets were being pumped up into a bubble. The report warned that a Mexico-style crisis could occur in Southeast Asia.

In May 1997, George Soros and other speculative fund operatives launched a series of attacks against the Thai baht. In June, LaRouche voiced the warning that a “very big crisis” was coming.

By summer 1997, the euphoric atmosphere began to evaporate fast. The currencies of Thailand and Indonesia were hit by severe speculative attacks, leading to major devaluations. During August, the Asian stock markets fell nearly continuously, while the New York Stock Exchange experienced wild oscillations.



*Lyndon H. LaRouche, Jr.: Apart from vague statements by some other economists, only LaRouche has clearly defined what a “New Bretton Woods system” should be, and what must be done to save the world economy from catastrophe.*

In September 1997, Lyndon LaRouche’s wife, Helga Zepp-LaRouche, visited India and China. In presentations to several economic institutes, she forecast that a financial crisis of enormous dimensions was about to occur in Asia, which would have profound effects for the entire global situation. She pointed especially to four elements: 1) the likelihood that “Mexico-style” collapses would break out simultaneously in several Asian countries; 2) the high probability of a new phase of the Japanese banking crisis, and the impact of losses due to Japanese loans to other Asian countries; 3) the likelihood that large investment funds, caught by a currency crisis, might quickly pull out of Southeast Asian markets; and 4) the effect of forced liquidations of assets by investors in one market, in order to cover losses in another market. Mrs. LaRouche warned, that the interaction of these four elements would lead to a crisis of unprecedented dimensions, and that the crisis would come very soon, almost certainly in October.

### **A ‘New Bretton Woods’ is the only way out**

The crisis which Mrs. LaRouche had warned about, actually did explode in late October. During the days following Oct. 20 (“Black Monday”), people everywhere got a little taste of what a sudden, global financial collapse could be like. A global chain reaction of market crashes was only avoided by massive intervention from the Federal Reserve and big U.S. corporations, to prop up the New York exchanges and prevent an uncontrollable panic. But the Southeast Asian countries became trapped in a vicious spiral of destruction of their currencies, financial systems, and national economies. That process has continued without interruption until now, in

spite of an unprecedented series of IMF “rescue packages”: \$20 billion for Thailand, \$45 billion for Indonesia, and \$57 billion for South Korea.

Meanwhile, the Japanese banking crisis continued to deepen. In November 1997 came the bankruptcies of the Hokkaido Takashuho Bank and Yamaichi Securities. On the same day, Japanese Prime Minister Ryutaro Hashimoto announced the biggest official rescue package in banking history — \$500 billion. The purpose, he said, was to prevent the Japanese banking crisis from leading to a world depression. Since then, however, the crisis has not stopped. A bottomless “black hole” has appeared in the Japanese financial system, which swallows up all money put into it, without ever filling up.

But, is the Asian financial crisis just an Asian crisis? For those who have studied the 30-year history which we have reviewed above, the answer is clearly negative: This is a world crisis, whose symptoms happened to break out first in the Asian region. Remember, from the very beginning until today, the Japanese bubble economy has been intimately linked with the bubble in the U.S. financial system. So also was the policy of pumping up the world financial markets with credit at nearly zero interest rates, in which the Japanese central bank played a key role. The huge flood of short-term foreign investment into “emerging markets,” which created most of the “miracle” of the “Asian tigers” in the years leading up to summer 1997, was not a healthy phenomenon; it was a manifestation of the metastatic phase of the global financial cancer.

In fact, it has become very clear, that the presently existing financial institutions, including the IMF and World Bank, can do nothing to stop the crisis from exploding again and again,



in ever more disastrous forms. The IMF policies, applied to the Southeast Asian countries, are destroying the economies of those nations and creating massive social instability; at the same time, the financial crisis has not been solved at all, but is actually developing toward a new explosion. This fact is broadly recognized among the leaders of Malaysia, Indonesia, and other countries.

Since the beginning of 1998, Lyndon LaRouche has repeatedly warned, that the policies being followed by the IMF, the U.S. Federal Reserve, and the Japanese government, to try to control or solve the crisis, threaten to unleash a process of hyperinflation in the world economy.

Speaking at a conference held on March 18 in Washington, D.C., LaRouche compared today's IMF policies to the Versailles Treaty after World War I, which led to the hyperinflationary crisis in Germany in 1921-23 and eventually to World War II. As LaRouche pointed out, at the time of the Versailles Treaty, the British economist John Maynard Keynes had predicted quite accurately what the effect would be. In spite of the warnings of Keynes and others, the Versailles policy was adopted, and the world was put on the track to disaster. LaRouche stated:

"Today, what is happening in Japan, and in the New York Federal Reserve System, is a piece of insanity, precisely like that against which Keynes warned in the Versailles Treaty. We are back to Versailles. The arbiter of the new Versailles, is a group of lunatics called the IMF bureaucracy. We have countries whose economies are collapsing. The IMF comes in and says, 'What you must do, is pay these creditors by shutting down your economy.' That was what they said in Korea, that is what they said in Indonesia, that is what they said in Malaysia, that is what they said in the Philippines, that is what they said in Thailand. That is what they said in Korea. Under these conditions, *none of these economies can ever recover*. None. *This is clinical insanity*. You can not find any basis under which financial reorganization of the type proposed by the IMF and accepted by most nations, can succeed. These kinds of proposals are simply the insanity of Versailles, re-enacted many times over. . . .

"And in the United States, we're pumping up a balloon, in terms of the financial markets, through hyperinflationary methods. The printing of money, to steer it into financial markets, where it is heavily financially leveraged, and thus results in an ascending balloon, in terms of the stock market prices. This creates the spectacle of a man clinging to a balloon, and without an oxygen flask, reaching the 60,000-foot level and going higher. He's going to suffocate and die, if the balloon doesn't explode. And, that's what we're doing."

Meanwhile, new crisis-spots are developing, in Russia, Brazil, and other some areas, which could become at least as dangerous as the Asian crisis of October 1997-January 1998.

More and more, people are realizing that the present financial system, including the IMF and related institutions, has come to an end. The voices are becoming louder, which

are calling for a fundamental reform, a "New Bretton Woods." Inside the U.S. government, for example, Treasury Secretary Robert Rubin speaks about a "new architecture" for the world financial system. Japan's Vice Finance Minister for International Affairs, Eisuke Sakakibara, has spoken directly about the need for a new international financial agreement along the lines of the original Bretton Woods System. In Europe, the same theme has been touched upon by several financial experts and political figures. Even George Soros has picked up this idea, and is trying to twist it around for his own evil purposes.

Apart from vague statements, only Lyndon LaRouche has defined clearly what a "New Bretton Woods" should be, and what must be done now to save the world economy from catastrophe in the coming period. In his March 18 speech in Washington, LaRouche said:

"There are three leading topics of interrelated financial, monetary, and economic policy-shaping, which must be considered as crucial for a true solution to the global, systemic crisis. . . .

"First, the fact that the present crisis is *global and systemic*, rather than *regional or cyclical*, must be acknowledged. . . . Those recent decades' institutionalized changes in policy, which are responsible for a three-decades build-up of the present crisis, especially since August 1971, must be identified, and entirely removed. That is, the changes made since approximately 1966-1967, in the policies of the U.S. government and the British government, the policies which became expressed by the 1967 collapse of the British pound sterling, the ensuing disorders in the dollar, the first step of collapse of the Bretton Woods System in March 1968, and then the collapse of the whole Bretton Woods System in August, mid-August 1971. . . . [Those policies] are the cause of what is today a global systemic crisis. It is not a cyclical crisis, it is not a business cycle crisis, nor is it regional. It is global. The entire system has destroyed itself; and the unravelling, which has taken over three decades, has now brought us to the end point, in which we either *eliminate* those policy changes which were popularized and institutionalized during the past three decades, or this world is not going to survive, in its present form. . . .

"Second, the present, fatally ill global financial and monetary system, must be radically reorganized. It can not be reformed, it must be reorganized. This must be done through the concerted actions of a key initiating group of governments. This must be done in the manner of a reorganization in bankruptcy, conducted under the authority of sovereign governments, not of international institutions.

"The acceptable model for the reorganized international monetary and financial system, is the incontestably superior, successful functioning of the old Bretton Woods System of the 1950s up to 1958-1959, compared to anything existing since those axiomatic changes in direction of policy-shaping were introduced by the United Kingdom and the United States, during the period 1966-1972.

“The required measures include:

- “a) periodically fixed exchange values of national currencies;
- “b) limited convertibilities, as may be required;
- “c) exchange controls and capital controls;
- “d) fostering of necessary protectionist measures in tariffs and trade regulations; and
- “e) outlawing of the creation of markets which conduct financial speculation against targetted currencies.

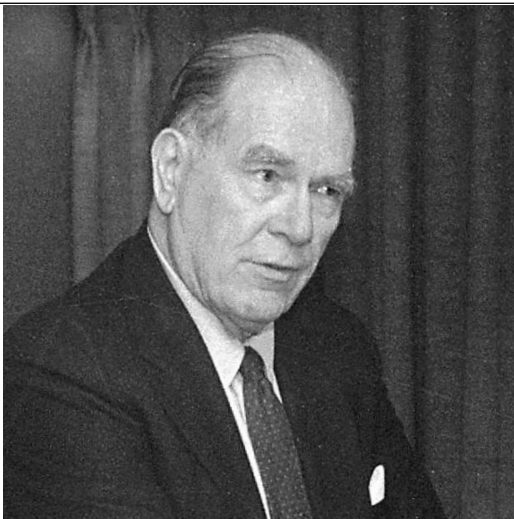
“Third, as measured in physical instead of the usual monetary terms, the world’s economy is presently functioning at levels of negative free energy, levels which are presently far below a breakeven point. The current levels of net physical output are insufficient to prevent the existing populations and economies from continuing to collapse into a spiral of accelerating general physical-economic contraction, and ultimate physical collapse.

“Unless this shortfall in per-capita physical output is reversed and soon eliminated, no financial and monetary system, however otherwise sound in design, could function. No mere medication could save a man who is being starved to death. There is no financial and monetary system which could possibly succeed, unless it were accompanied by a general program of forced physical-economic recovery, a program which must rapidly approach and reach the levels of sustain-

able, positive free-energy ratios. This means a recovery analogous in important respects to the Franklin Delano Roosevelt recovery in the United States, and on a global scale.”

LaRouche emphasized, that the key to a real recovery of the world economy, in terms of physical economy, is to realize large-scale infrastructure projects throughout the world. These projects provide a basis for expanding cooperation and trade between industrial and developing nations. They should employ the most modern technologies, and be used not only to provide the essential transport, energy, water, communications, and other infrastructure to underdeveloped areas, but also to stimulate the growth of modern, capital-goods industries and the development of new technologies in every country. The Eurasian Land-Bridge, with its connections throughout Europe and Asia, as well as Africa, would be a centerpiece of that effort. For that purpose, the policies and methods of the American System, which were pioneered under Abraham Lincoln and Henry Carey, to build up the U.S. infrastructure and industry in the second half of last century, are the best existing model for what must be done on a global scale today.

The crucial issue which LaRouche raised, however, is the question of leadership: Will the nations and governments of the world find the political will and determination, to make sure that the necessary measures will be realized? That is the challenge, which we now leave for our readers.



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Anchorage . . . . . 1300	Buenos Aires . . . . . 1900	Honolulu . . . . . 1200	Los Angeles . . . . . 1400	Pittsburgh . . . . . 1700	Teheran . . . . . 0130*
Athens . . . . . 2400	Buffalo . . . . . 1700	Hong Kong . . . . . 0600*	Madrid . . . . . 2300	Prague . . . . . 2300	Tel Aviv . . . . . 2400
Atlanta . . . . . 1700	Cairo . . . . . 2400	Houston . . . . . 1600	Manila . . . . . 0600*	Rangoon . . . . . 0430*	Tokyo . . . . . 0700*
Auckland . . . . . 1000*	Calcutta . . . . . 0330*	Istanbul . . . . . 2400	Mecca . . . . . 0100*	Richmond . . . . . 1700	Toronto . . . . . 1700
Baghdad . . . . . 0100*	Caracas . . . . . 1800	Jakarta . . . . . 0500*	Melbourne . . . . . 0800*	Rio de Janeiro . . . . . 1900	Vancouver . . . . . 1400
Baltimore . . . . . 1700	Casablanca . . . . . 2200	Jerusalem . . . . . 2400	Mexico City . . . . . 1600	Rome . . . . . 2300	Vladivostok . . . . . 0800*
Bangkok . . . . . 0500*	Chattanooga . . . . . 1700	Johannesburg . . . . . 2400	Milan . . . . . 2300	St. Louis . . . . . 1600	Venice . . . . . 2300
Beijing . . . . . 0600*	Chicago . . . . . 1600	Karachi . . . . . 0300*	Minneapolis . . . . . 1600	St. Petersburg . . . . . 0100*	Warsaw . . . . . 2300
Belfast . . . . . 2200	Copenhagen . . . . . 2300	Kennelbunkport . . . . . 1700	Montreal . . . . . 1700	San Francisco . . . . . 1400*	Washington . . . . . 1700
Berlin . . . . . 2300	Denver . . . . . 1500	Kiev . . . . . 2400	Moscow . . . . . 0100*	Santiago . . . . . 1800	Wellington . . . . . 1000*
Bohemian Grove . . . . . 1400	Detroit . . . . . 1700	Khartoum . . . . . 2400	New Delhi . . . . . 0330*	Sarajevo . . . . . 2300	Wiesbaden . . . . . 2300
Bogota . . . . . 1700	Dublin . . . . . 2200	Lagos . . . . . 2300	New York . . . . . 1700	Seattle . . . . . 1400	Winnipeg . . . . . 1700
Bonn . . . . . 2300	Gdansk . . . . . 2300	Lima . . . . . 1700	Nogales . . . . . 1500	Seoul . . . . . 0700*	Yokohama . . . . . 0700*
Bombay . . . . . 0330*	Guadalajara . . . . . 1600	Lincoln . . . . . 1600	Norfolk . . . . . 1700	Shanghai . . . . . 0600*	Yorktown . . . . . 1700
Boston . . . . . 1700	Havana . . . . . 1700	Lisbon . . . . . 2300	Oslo . . . . . 2300	Singapore . . . . . 0530*	

\* Mondays