Clinton takes the lead on new financial architecture

by William Jones

Speaking to the Council on Foreign Relations in New York on Sept. 14 in his first major policy speech since his Aug. 17 testimony before independent counsel Kenneth's Starr grand jury, President Bill Clinton put himself in the forefront of a renewed drive to revamp the international financial system. "Today, I have asked Secretary [Robert] Rubin and Federal Reserve Board Chairman [Alan] Greenspan to convene a major meeting of their counterparts within the next 30 days to recommend ways to adapt the international financial architecture to the 21st century," the President said.

"If you consider today's economic difficulties, disruptions, and plain old deep personal disappointments of now tens of millions of people around the world, it is clear to me that there is now a stark challenge not only to economic freedom but, if unaddressed, a challenge that could stem the rising tide of political liberty as well," the President warned.

"For most of the last 30 years, the United States and the rest of the world has been preoccupied by inflation, for reasons that all of you here know all too well," Clinton said. "But clearly the balance of risks has now shifted, with a full quarter of the world's population living in countries with declining economic growth or negative economic growth."

This is not the first time that President Clinton has placed the global financial crisis on the agenda. Already in June 1995, at the Halifax summit of the Group of Seven (G-7) leaders, restructuring the international financial system became the main item of discussion, after President Clinton put the topic on the agenda at the previous G-7 meeting in Naples. At Halifax, however, in an attempt to try to balance often opposed political and financial viewpoints represented at the meeting, the leaders' communiqué limited itself to a call for greater supervision by, and more funding for the International Monetary Fund (IMF). In fact, however, it has been the very policies of the IMF which have seriously aggravated the crisis, leading to the effective bankruptcy of the IMF itself and an imminent breakdown of the global financial system.

Threat to U.S. economy is clear

All too often, when asked to comment on the economic situation in the United States, President Clinton's typical response has been to reference the latest figures that someone has slapped together in order to show how great things were going with the U.S. economy. In the last couple of months, however, with the disastrous effects of the Asian crisis throwing key sectors of U.S. industry into turmoil, such figures have been much more difficult to conjure up. Accordingly, the President's comments on the economy have become increasingly less sanguine. Now it is clear that such tinkering with the system will not be sufficient, and that the U.S. economy is directly threatened by the crisis.

With the economies of Asia threatened by growing economic chaos, leaders of the Asian nations prevailed upon the U.S. President in November 1997 at the Asia-Pacific Economic Cooperation forum, to take the initiative in convening a meeting of finance ministers from the G-7 countries and from the nations hit by the crisis, to discuss reforming the global financial system. The President agreed to their proposal, and, at the invitation of Treasury Secretary Rubin, the finance ministers and central bank governors of 22 nations, including Russia and India, met in April of this year at the Madison Hotel in Washington to discuss these issues.

The Group of 22 includes China and Hong Kong, Japan, South Korea, Indonesia, Malaysia, Thailand, and Singapore; India and Australia; Canada, Brazil, Argentina, Mexico, as well as the United States; and France, Germany, Italy, Britain, Russia, and Poland. And, South Africa.

At the same time, Lyndon LaRouche was garnering increasing international and national support for his call to President Clinton to convene a New Bretton Woods conference, which could lay the basis for a real alternative to the bankrupt IMF system. Seeing the insanity of trying to conduct piecemeal reform as the system was fast sinking, LaRouche called upon the President to bring together the heads of the most important economic nations, particularly Russia and China, to establish a system of fixed parities among the nations' currencies, which would facilitate trade and investment. Although the issue of exchange rates and currency controls was broached at the G-22 meeting in April, after several hours of heated discussion the ministers and central bank governors decided to put off any resolution to these contentious questions and to set up three working groups which would put forward proposals at a yet undetermined meeting in the future.

The time has come

Since the April meeting, however, little has been done. Instead, the subsequent collapse of the Russian ruble, and the refusal of the Japanese to write off much of the bad debt now encumbering their banking system, have threatened to topple world markets. The recent measures taken by Malaysia and Hong Kong to protect their markets against the ravages of the hedge funds, underlines the need of a global solution to the problem.

At the proverbial eleventh hour, the President decided to turn his attention to the global systemic crisis. With finance ministers and central bank governors heading to Washington for the annual IMF meeting at the end of September, the time is propitious for reviving the G-22, or perhaps a broader gathering, with which to move forward on the creation of the new financial architecture.

President Clinton underlined the vital interest the American people had in dealing with this global crisis. "These people are our customers. With one-third of the growth of our economy coming from exports, much of it from emerging markets, we know that those markets will falter as their economies flatten. When the problem is widespread and perceived to be moving in the wrong direction, we have seen that our stock market can react, having a direct and immediate impact on the wealth of the American people."

"This is the biggest financial challenge facing the world in a half century," Clinton said, "and the United States has an absolutely inescapable obligation to lead and to lead in a way that's consistent with our values and our obligation to see that what we're doing helps lift the lives of ordinary people, here at home and all around the world."

In a reference that caught the ear of those listening to LaRouche, the President made an unusual reference to the FDR era. "The World War II generation did it for us 50 years ago. Now it is time for us to rise to our responsibility as America has been called upon to do so often, so many times in the past. We can, if we do that, redeem the promise of the global economy and strengthen our own nation for a new century."

President Clinton outlined six short-term measures to alleviate the problems. "Concerted action to spur growth, helping Asia through private-sector debt restructuring and a strengthened social safety net, helping to protect the rest of the world through the use of the IMF's emergency fund, increasing the activity of the ExIm Bank, and meeting our own obligations to the IMF—these are the six immediate steps we want to take," Clinton said.

IMF hangover

While the President's proposals implicitly criticize IMF policies, Clinton unfortunately still promoted that bankrupt institution, and its nostrums on free markets and free trade. He went on to urge the need to rapidly deal with the long-term, systemic problem. "I just want to emphasize that even as we respond to the urgent alarms of the moment," he said, "we must speed the pace of this systemic work as well. . . . We must also be willing to take action for the long run, to modify the financial and trading institutions of the world to match the realities of the new economy they serve."

"We must develop current policies so that countries can reap the benefits of free-flowing capital in a way that is safe and sustainable," said Clinton. "We must adapt the IMF so that it can more effectively confront the new types of financial crises, minimizing their frequency, severity, and human cost. We need to consider ways to extend emergency financing when countries are battling crises of confidence due to world financial distress as distinct from their own errors in policy. We must find ways to tap the energy of global markets without sentencing the world to a cycle of continued extreme crises."

People over markets

Shortly thereafter, the President again referenced his proposal at a group of Democratic supporters at a "Unity '98" luncheon in New York City. "You know, after the Great Depression in America we learned how to limit the swings of the economy and [we] haven't had another depression. And it stabilized things. We have to do that in the world," the President said. He continued, "We've got to make the global economy more humane. We have to make it work for ordinary people. And when times are tough and countries have to go through difficult times, we've got to help the innocent and make sure they don't get punished too badly. Otherwise, the support for free markets and democracy will erode."

In a press conference following the President's speech, Treasury Secretary Rubin and National Economic Council director Gene Sperling elaborated some ideas on the kind of debt restructuring that would help get credit flowing. Both emphasized a systemic approach. Rubin said that it is not totally effective "to deal with this enterprise-to-enterprise, but that it would be useful to have a more systematic way to deal with these kinds of issues." Sperling was even clearer: "So, the goal is to explore whether there are comprehensive approaches that would give incentives for all the players—for the banks, for other creditors and the companies—to try to get this debt overhang out of the way so that they could begin getting new capital and investing and expanding."

This approach seems to go in the direction of the bankruptcy reorganization proposals LaRouche has often proposed. But the acute, terminal nature of the present systemic crisis requires that any "new architecture" take on the fundamental features of the LaRouche "New Bretton Woods" proposal, which is gaining wide support throughout the world.

Global collapse demands a New Bretton Woods

by William Engdahl

A banker with one of the largest European banks told *EIR,* "I am now convinced the world is coming into currency and capital controls, to a new Bretton Woods as Mr. LaRouche calls it, as the only way to save things." The banker added, "Clinton's New York speech to the Council on Foreign Relations is very important in this light. The American President is the only one who can make such a call. It should have been made before Russia's crisis, but better late than never."

Remarking on the content of Clinton's CFR speech, he noted, "Re-organization of the IMF [International Monetary Fund], development of a new architecture similar to the original idea of Bretton Woods, these are big proposals which Clinton now has put on the table. This is the response I have been looking for for some time. It at least signals an attempt by the President to try to forge some consensus on the crisis."

By all indications, the President's call for an emergency meeting of the Group of 22, an ad hoc gathering which met first in April in Washington, to consider measures to deal with the growing global financial and economic crisis which broke out in Asia, comes not a minute too soon.

While major stock markets of the Organization for Economic Cooperation and Development (OECD) industrial countries appeared for several days in mid-September to have momentarily recovered some lost ground, following drastic plunges of several weeks, the global economic crisis had gathered momentum, with prospects of a financial system blowout likely to erupt at any moment.

Japan at the center of the crisis

On Sept. 17, Tokyo's Nikkei Dow stock index fell to 13,800, its lowest level in 12 years. Japanese banks calculate the market value of their core, or permanent stock holdings in related companies, the Japanese Keiretsu, two times per year, on March 31 and Sept. 30. At a Nikkei level of 14,800, the OECD estimates that these hidden stock assets of Japan's 19 largest banks fall to zero, or become a loss for the banks' balance sheets. The severe slide in the Nikkei, should it last until Sept. 30, is likely to force several banks below the internationally mandated Bank for International Settlements' 8% bank capital ratio, fuelling new fears of a Japanese banking meltdown.

The proximate trigger for the Nikkei slide in recent days was the failure of the Obuchi government to come to a compromise with the opposition-controlled Upper House of Parliament, on emergency measures to deal with country's estimated $2 trillion in bank bad loans. The size of the problem is so mammoth, that it defies attempts to deal with it within the current, bankrupt financial system. "I am very pessimistic on Japan," commented Alex Balfour, manager of a London-based fund specializing in Japan. "The Bank of Japan last week cut call-money interest rates to 0.25%, as an act of sheer desperation over the continuing policy paralysis of the government. It was an attempt to shame the government into acting. The economy is collapsing, housing starts are down 40%, bankruptcies are soaring to a postwar record."

Even without a new phase of Japan bank crisis, the first-ever default by a sovereign debtor, Russia, on its foreign and domestic loans in late August, has set off global shock waves, which are far more awesome than anyone admits openly. By defaulting only weeks after the IMF gave it an unprecedented $22.6 billion rescue package, and after the United States had backed it up, Russia has let fund managers around the world know that the "impossible" is possible. The result has been a universal collapse of confidence in "crisis management" techniques, leading to a severe contraction of investment in every market around the world considered even remotely risky.

Russia default hits Brazil

"By casting doubt on the integrity of all emerging and developing debt, [Russia's default] has triggered a global margin call and credit crunch," David Hale, chief economist of Zurich Insurance, told *Barron's* on Sept. 14. "As a result, interest rates have soared in places like Brazil, Mexico, and Venezuela, raising the specter of a recession in 1999 in a continent which is a major trading partner of the United States." The Russia default has hit Brazil "like a tornado," says Hale, driving interest rates to almost 50% in a desperate bid to prevent devaluation of the Brazilian currency, the real, or at least postpone it until after the Oct. 4 Presidential elections.

"My major worry right now is Latin America, especially Brazil," a senior director of one of Europe's central banks stressed to with *EIR.* "Brazil faces elections, and its short-term dollar debts coming due in the next three months are very, very high. If Brazil begins to have frictions, then the world has real problems. It is the largest economy in Latin America and a major U.S. trade partner."

Adding to worries over Brazil is the growth of flight capital. In the first two weeks of September, more than $13 billion left Brazil, almost $1 billion daily, forcing the Central Bank to hike interest rates to 49.75%, up from an already high 29.75%. The Brazil government has let itself become hostage to its foreign creditors for the second time in two decades. In August, $12 billion left the country. Brazil foreign currency reserves have fallen to $452 billion. Between now and Dec.