New Solidarity International Press Service

IPS Weekly Financial Newsletter

International Market News

Japan, Saudi Arabia Take Steps to Move Out of Dollar Orbit

Oct. 25 (IPS) -- Japan, Saudi Arabia, and possibly Great Britain have taken important steps this week to move out of the orbit of the bankrupt dollar, insuring an early displacement of the dollar as the international reserve and trade currency. In a related development, the Bundesbank, West Germany's central bank, decided yesterday to break with the U.S. Federal Reserve Chairman Arthur Burns-inspired policy of supporting the dollar.

First, the Japanese decided to issue low-interest credits to the Soviet Union and participate in the Siberian oil development project without any U.S. participation. The question of U.S. participation had deadlocked negotiations on the project for two years. Next, Japan signed a $1 billion oil-for-technology deal with pro-Soviet Iraq early this week. Negotiations are now in progress for a similar deal between Japan and Saudi Arabia.

Even more significantly, the Japanese made moves this week towards "triangular" trade arrangements with the developing sector. Japan and India signed a deal under which the Japanese will help India double its rice production using sophisticated Japanese water-management techniques. This process would enable India to meet most of Japan's food needs. The Japanese have also committed themselves to increasing Indian steel production. In addition, the Japanese and Indians have agreed to cooperate on joint development projects in "third countries" in the Mideast.

Such development deals carry with them the necessity of developing a stable international currency for the settlement of accounts to replace the bankrupt dollar -- a role which only the Soviet transfer ruble can possibly take on.

The Arabs and the British

After three days of intense negotiations between a high-level Saudi delegation and representatives of the British government, the two have signed a 350 million-pound trade contract. The signing of this contract has essentially saved Great Britain from receivership at the hands of the International Monetary Fund (IMF). The Fund had duly informed Britain that should the country come to it for a bailout loan, it would have attached harsh "MAC"-type budgetary control and austerity measures to all further financing to that country. At the signing of the Saudi-British trade and development deal, the Saudis pledged their determination in maintaining a strong and economically viable Europe. They also expressed concern over the growing gap between the developed and developing countries and recognized the necessity of joint Saudi-British efforts for the establishment of a "new world economic order."

According to highly reliable sources, the Saudis have also made low-interest credits available to France and West Germany and are negotiating for a $1 billion loan to Italy. The Saudi moves are expecially important in light of their key role along with Algeria in pushing for discussion of monetary questions at the recently concluded North-South Conference in Paris. The U.S. vehemently opposed discussion of any monetary questions at the meeting.

The Germans Move Away From the Dollar?

Yesterday, the Bundesbank announced that it will stop intervening in the domestic capital markets and purchasing government debt to artificially depress short-term interest rates. The previous Bundesbank policy had resulted in huge capital outflows into the higher-interest paying dollar sector. At the same time, the Bundesbank lowered its discount rate by half a percentage point to ensure that short-term interest rates do not get out of hand.

The decision to halt outright Bundesbank purchases of government bonds will result in higher domestic short-term interest rates and make it attractive for German depositors to maintain their funds in the Deutsch Mark sector. In turn, the new policy will deny desperately needed funds to the illiquid dollar sector.

More importantly, however, the decision represents a clear break on the part of West Germany from a policy of supporting the illiquid dollar at the expense of West German industry and trade.

Foreign Exchange Market Reactions

On Wednesday, Oct. 22, the day the British-Saudi negotiations concluded, Kuwaiti investors reportedly bought "unusually large" amounts of sterling, resulting in a 1.5 cent appreciation in the pound against the dollar. The same traders who had expected the pound sterling to go down to the $2 level admitted that the pound would now rise to $2.10 in a matter of days.

The same day, the Deutsch Mark hit a three-month high and the French Franc a two-month high against the dollar. Additionally, there were large spot sell orders for dollars from Western Europe, reversing the short-term inflow of funds into the dollar sector. Even the major New York banks started to go short on dollars in a big way.

Had it not been for the large interventions on the part of the central banks of Switzerland, Belgium, West Germany, and France, the dollar would have weakened dramatically. At this point, central bank interventions on behalf of the dollar are the only supports the dollar has. As most bankers realize, such support operations cannot be effective much longer.

Yen Stabilizers

This week saw the firming up of the Japanese Yen as Japanese banks joined European and New York-based bankers in betting against the dollar on the forward market. Spot activity has been quiet all over the world, and especially in Tokyo, where the Bank of Japan is actively supporting the use of Yen for the settlement of Japan's international accounts. Presently, Japan settles 99 per cent of its import transactions and 90 per cent of all export transactions in dollars. In contrast, West Germany conducts 80 per cent of its trade in DMs, and Italy 50 per cent of its trade in Lira.

And in the Cuckoo's Nest

A highly placed source at the Federal Reserve Bank in Washington has disavowed recent statements by Federal Reserve Bank governor Henry Wallich in Frankfurt and investment banker Robert Roosa in Tokyo that the U.S. should support the idea of an actively managed floating rate regime in the form of a dollar, DM, and Yen zones. These statements have absolutely nothing to do with official U.S. policy, the source said. "If we agree to support any such system, it would rapidly drain our reserves and add to our debts." Support of such a scheme would quickly force the bankrupt U.S. treasury into receivership.